

REDACTED – FOR PUBLIC INSPECTION
Pursuant to Protective Order in CC Docket No. 01-338 & WC Docket No. 04-313

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of)	
)	
Unbundled Access to Network Elements)	WC Docket No. 04-313
)	
Review of the Section 251 Unbundling)	CC Docket No. 01-338
Obligations of Incumbent Local Exchange)	
Carriers)	
)	

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EXECUTIVE SUMMARY

In this remand proceeding, AT&T no longer seeks permanent rules that require the unbundling of mass market switching and the maintenance of UNE-P. Rather, AT&T proposes only those unbundling rules that are needed to foster *facilities-based* competition through competitively provided switches, fiber rings, and other local network facilities. This is the competition the Commission has pledged to promote. But this competition will fail unless competitive carriers have cost-based access to the high capacity “last mile facilities” – loops, transport, and loop-transport combinations (EELs) – that are required to connect end user locations to competitive carriers’ networks and that cannot be economically obtained outside the incumbents’ networks.

AT&T thus urges the Commission to adopt rules that do two basic things. *First*, it should grant competitive carriers unbundling rights to loops with up to 2 DS3s of capacity and to dedicated transport (including entrance facilities) with up to 12 DS3s of capacity. In particular, the massive records compiled in the state impairment proceedings and in this remand proceeding have now filled the gap in the evidence that had existed on these points in the prior *Triennial Review* proceedings. The record now establishes that, with only *de minimis* exceptions, competitive carriers have no ability to obtain economic alternatives below these capacity thresholds anywhere in the country. Indeed, even when competitive carriers have demand that exceeds these capacity thresholds, there are many circumstances where it is uneconomic for them to build their own alternative facilities. The facts thus compel a national impairment finding for loops and transport below these capacity levels, with (at most) exceptions on the few routes where multiple wholesalers can certify that they provide alternatives.

Second, the Commission should eliminate or modify its “eligibility” restrictions that prohibit the use of loop-transport combinations (EELs) to provide long distance and certain local

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services. Access to these last mile facilities is essential to the provision of long distance services, and a fundamental intervening change in conditions – the Bells’ entry into the enterprise long distance market – now requires that these facilities be available as UNEs to all providers of long distance and other landline services. In particular, now that Bells are providing interexchange services to enterprise customers, IXC’s and CLEC’s alike will be severely impaired if all competitive carriers cannot obtain access to the Bells’ essential last mile facilities at economic costs that are similar to those that the Bells incur. At a minimum, the Commission’s new rules should end the eligibility restrictions for all long distance and other services that are offered in the future under new or renewed contracts, as well as for all EELs used to provide any local service.

Both sets of rules are essential to achieving the objects of the 1996 Act. Without such rules, incumbent LECs would have licenses to maintain their monopolies over local services to enterprise customers, *and* to further extend those monopolies into markets for enterprise long distance services, eliminating the robust competition that developed over the past two decades.

AT&T’s proposed rules fully respond to the D.C. Circuit’s decision in *USTA II*. Indeed, each of them rests on features of the *Triennial Review Order* or other factors that the Court expressly approved or endorsed in *USTA II*. By contrast, while the Bells have attempted to swamp the Commission with “new evidence,” their “data” are either irrelevant to the decisions the Commission must make or directly support AT&T’s proposals.

National Impairment Findings For Loops And Transport Below The Specified Capacity Thresholds. First, AT&T proposes that the Commission adopt a national impairment finding for loops with up to 2 DS3s of capacity and for transport with up to 12 DS3s – specifically including all DS1 level facilities. In the *Triennial Review Order*, the Commission

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had made provisional impairment findings in these precise conditions. It had adopted an impairment standard that asked whether there are barriers to entry if competitors are denied access to a network element that arise from the existence of natural monopoly characteristics, sunk costs, absolute cost differences or other structural impediments to competitive supply. It also concluded that impairment determinations must be made on a capacity-specific and carrier-specific basis. And while the Commission found that the *Triennial Review* record was insufficient to determine whether competitive supply below the capacity thresholds levels is economic under conditions in particular local markets, the Commission concluded that this record established that impairment generally exists below the 2 DS3 and 12 DS3 thresholds – including for all DS1 facilities.

USTA II did not fault *any* of these specific determinations. Rather, it expressly endorsed the Commission's basic impairment test, provided that the Commission clarify (as it should now) that the test focuses on the effects of entry barriers on *efficient* requesting carriers. The Court also did not question the *Triennial Review Order's* determination that impairment determinations for high capacity elements should be both capacity- and carrier-specific. Nor could it have. It is undisputed that loop and transport transmission facilities are characterized by very high fixed costs and scale economies, and that no competitive carrier can make these enormous fixed and sunk investments unless it has sufficient demand to make the investment economic on a route.

Further, although the Court of Appeals vacated the Commission's delegation of unbundling authority to the states, it found nothing wrong with the *Triennial Review Order's* unanimous national finding of impairment for all DS1 loops and all for DS3 loops with less than 3 DS3s of capacity. But the Court advanced narrow objections to aspects of *Triennial Review Order's* impairment findings for transport. Each can be readily addressed by the Commission.

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National Impairment Findings. *USTA II* first held that the *Triennial Review Order*'s national impairment finding for dedicated transport below 12 DS3s could not stand after the "safety valve" provided by the state impairment proceedings was eliminated. The Court here relied on the ground that the *Triennial Review Order* had *disclaimed* that it had a sufficient factual basis to make a national impairment finding. In particular, the Court noted that the *Triennial Review Order* stated that the Commission lacked sufficient evidence to determine the extent to which competitive carriers had (or could) economically provide alternative transport facilities at lower capacity levels in any specific local markets, and thus expressly "doubted" that there was a basis in the *Triennial Review* record for a non-provisional national impairment finding for transport. *USTA II*, 359 F.3d at 574.

As explained in detail in AT&T's comments and supporting declarations, all such "doubts" have been eliminated because any prior evidentiary gap has now been completely filled. The state impairment proceedings established – and the record here confirms – that the capacity thresholds very closely track the actual circumstances in which alternative facilities have been deployed. For example, the state data show that, even in the densest urban areas, there are only a *de minimis* number of cases where competitors have been able to construct (or to find wholesale) alternatives below these capacity levels. The actual data show there are collectively only 130 buildings in 12 states (including California, Texas, Florida and Illinois) that have two or more self-providers of loops with less than 2 DS3s of capacity, and fewer than 50 buildings – in all those states combined – where wholesale DS3 or DS1 loops are available. Similarly, the state data show there are only a total of 55 transport routes in 14 states (including all the above states plus New York) with three or more self-providers of DS3 transport and fewer than 50

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routes in all of those states where there are two or more wholesalers of DS3 or DS1 transport. This is a miniscule fraction of one percent of the total possible transport routes in those states.

Most fundamentally, the evidence here definitively proves that any future construction at or below the 2 DS3 and the 12 DS3 thresholds would be uneconomic for an efficient competitive carrier using the most efficient technology. The only exceptions that would exist are in highly unique circumstances from which no generalizations can be drawn: *e.g.*, where a building happens to be a few feet from an access point on a competitive carrier's network.

And there is simply no contrary evidence. While the Bells have attempted to deluge the Commission with color-coded maps and other "data," this information actually supports AT&T's proposals. The Bells' "fiber maps" themselves show that in the vast majority of circumstances competitive carriers depend on the *Bells* – not competitive carriers – to reach individual customer locations. And in the limited instances where competitive carriers have deployed fiber, the Bells' maps make no attempt to identify the *capacity* of the services being provided over those facilities. Thus, as detailed below, this information merely confirms what the Commission already found – that deployment of transport and loops *above* the specified capacity thresholds is sometimes economic. And in all events, the Bells provide absolutely no evidence that competitive carriers are not impaired *below* these thresholds.

Wholesale Trigger. While competitive carriers may not be impaired on a route where there is a viable competitive wholesale transport market, the Commission correctly concluded in the *Triennial Review Order* that there must be at least two wholesalers before there can be a finding of non-impairment – and the Court of Appeals in *USTA II* did not disagree. But there is no need for the Commission to adopt a wholesale trigger here or otherwise to provide for a wholesale exception to its national impairment findings.

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It is elementary that national rules are to represent conditions that are “widespread” (*USTA II*, 359 F.3d at 569), that “*some*” overinclusiveness is inevitable in all rules (*id.* at 570), and that “administrab[ility]” is a valid factor in establishing unbundling rules (*id.* at 576). That is particularly so because the Court expressly “assumed” that the “at a minimum” clause of § 251(d)(2) authorizes rules that require unbundling even in conditions where impairment does not exist if there is good cause for the requirement. *USTA I*, 290 F.3d at 425. Given the *de minimis* amount of competitive wholesaling and the severe impediments to the provision of wholesale services by competitive carriers (discussed in detail below), the Commission’s rules need not account for the existence of wholesale services. But if it chooses to do so, the most the Commission should consider is a rule that denies unbundling on routes where the wholesalers themselves certify that they are providing in fact providing wholesale DS1 and DS3 transport.

Market Definition For Transport. *USTA II* also made narrow and hypertechnical criticisms of the *Triennial Review Order’s* adoption of point-to-point routes as the relevant market for making impairment determinations for transport and not (as the incumbents proposed) Metropolitan Statistical Areas (MSAs). While acknowledging that it “may be infeasible to define the barriers to entry in a manageable form” that could be applied to MSAs or other broader geographic markets, the Court faulted the Commission for “nowhere suggest[ing]” that it had explored such alternatives or found them inferior to a route-by-route analysis because of their higher “error costs” in terms of “false positives” and “false negatives” or otherwise. *USTA II*, 359 F.3d at 574-75.

The Commission can readily address this hypertechnical point. There is no dispute that transport markets are point-to-point routes. The Bells’ own economists have for years contended – correctly – that the markets for special access services (and thus correlatively for UNEs

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comprised of the same facilities used in special access services) are point-to-point. In all events, the evidence clearly shows the reason why it is necessary to use point-to-point routes when making impairment determinations for high capacity loop and transport facilities. Competitive carriers must make entry decisions on a route-by-route basis. The question whether it is economic to deploy transmission facilities turns on the demand a carrier expects to service on that *individual* route and whether that demand is sufficient to cover the fixed and sunk investments specific to that route.

Conversely, the evidence shows that the incumbents' MSA proposal would be replete with "false negatives" – findings of non-impairment where impairment is clear. By contrast, as shown above, the state data show that applying the capacity limits on a route by route basis identifies virtually all situations where there is "no impairment." As shown above, the capacity/route test also results in at most *de minimis* "false positives" – findings of impairment where there is none. And while there are conditions in which impairment in fact exists *above* the capacity thresholds (*e.g.*, if rights of way or building access are unobtainable), this does not at all affect the propriety of using the capacity/route test to identify clear cases of *impairment*.

USTA II similarly faulted the *Triennial Review Order* for allegedly concluding that the existence of competitive deployment on one route is irrelevant to a determination as to whether competitive carriers are impaired without access to transport on a second route where the competitive carrier allegedly faced the same or similar entry barriers. The Commission can and should clarify that such evidence is not irrelevant, and it should make explicit that it took any such circumstances into account in finding that impairment exists below the specified capacity thresholds. In particular, the capacity test determines the routes on which deployment of alternative facilities is and is not economic, and thus determines what routes are and are not

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“similarly situated” in terms of the entry barriers that a competitive carrier faces. Correlatively, the evidence now shows that there has been only *de minimis* deployment below the 2 DS3 and 12 DS3 capacity thresholds, and that where such deployment occurred in the past, it was uneconomic and in no way indicates that alternatives would exist on other routes where the capacity thresholds are not met.

Entrance Facilities. *USTA II* remanded the Commission’s rule denying competitors access to the subcategory of dedicated transport known as “entrance facilities,” which provide the last link between an incumbent’s network and a competitive carrier’s network. The Court held that these facilities are “network elements” and that the Commission’s rules may not deny unbundled access to them unless it finds a lack of impairment on remand. The evidence demonstrates that the economics of constructing entrance facilities are identical to those that apply to other transport facilities. Thus, impairment must be found for any entrance facility with 12 or fewer DS3s of capacity.

The Irrelevance Of Special Access To Impairment Determinations For Elements Used In Landline Local and Long Distance Services. Because of the overwhelming evidence that self-supply of loops and transport is uneconomic below the specific capacity thresholds, the Bells have shifted their focus. They now primarily contend that their offers of tariffed special access services at above-cost rates eliminate the impairment that would otherwise exist for these facilities. They note that the Commission’s use/eligibility restrictions (and the incumbents’ “no facilities” policies) have barred access to high capacity loops and transport as UNEs, and they contend that interexchange carriers and other competitive carriers have “thrived” using special access to provide long distance and certain local services to enterprise customers.

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This claim does not withstand even cursory scrutiny. Congress enacted § 251(c)(3) and provided for cost-based access to UNEs precisely because incumbents would otherwise have the ability and incentive to price and provision tariffed services to effect price squeezes or otherwise to foreclose competition on the merits with incumbent-provided services. Here, the evidence shows that Bells' high special access rates and poor provisioning have already foreclosed competitive carriers from providing an array of local landline services. Indeed, there are many instances in which the incumbents' tariffed special access rate itself exceeds the price of the incumbents' retail local service, and there are many other situations where the incumbents' special access rate is so high that competitive carriers would lose money if they attempted to offer retail services in competition with the incumbents.

Because the Bells are now able to provide long distance service to enterprise customers, the Bells will have both the incentive and the ability to effect price squeezes for virtually *all* local and long distance services used by enterprise and other business customers if competitive carriers are hereafter relegated to special access service and denied access to high capacity loops and transport as UNEs. The reality is that federal and state special access regulations afford no protections against price squeezes and similar incumbent LEC abuses. It is thus axiomatic that the existence of tariffed special access affords no basis to deny competitors access to UNEs where they otherwise are impaired.

The Bells' contrary claims rest on ground that *USTA II* vacated the Commission's rule that had treated special access as irrelevant to all impairment determinations. But they ignore that the rule had been applied only to grant UNE rights to CMRS carriers, notwithstanding the unique character of wireless services and the undisputed fact that CMRS providers had been profitably providing wireless service in competition with incumbents for 20 years by obtaining

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the incidental transport facilities used in wireless networks under special access tariffs. *USTA II*, 359 F.3d at 575-76. Further, the Bells also ignore that *USTA II* expressly stated that the Commission’s prior rule may be re-adopted on remand and that the Commission may treat special access as irrelevant to impairment determinations for landline services where incumbents have the ability and incentive to effect price squeezes or similar abuses. *Id.* at 576-77.

The Court recognized that there is an obvious “risk of ILEC abuses” if competitive carriers are limited to tariffed special access services (*id.* at 577), noting the “ILECs’ incentive[s]” to set the special access prices “as high as possible” relative to their retail rates. *USTA II*, 359 F.3d at 576. Because of “the vagaries of determining when th[ose] price[s] get[] so high that the ‘impairment threshold’ has been crossed,” the Court also acknowledged that assessing the competitive significance of special access could raise “real administrab[ility] issues” and that that “these complications” themselves could “support a blanket rule treating the availability of ILEC tariffed services as irrelevant to impairment.” *Id.* Further, the Court recognized that tariffed special services “present different opportunities and risks for the requesting carrier than the use of UNEs” and that the Commission may find that these differences will create impairment if competitive carriers are limited to special access for their landline or other services. *Id.* at 577.

In the case of landline services, these considerations require that the Commission either re-adopt the rule that treats the availability of special access as irrelevant to impairment determinations or find that special access is insufficient to eliminate the impairment that otherwise exists for loops and transport below the capacity thresholds. Special access inherently creates risks of price squeezes for all landline services. In addition to the fact that there are performance plans and standards for UNEs – and not for tariffed special access services – UNEs

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alone provide the assurances of cost-based rates and of rate stability that competitive carriers must have if they are to bid on the multi-year contracts that enterprise customers require. Month-to-month special access rates are greatly in excess of cost and provide no stability. To the extent special access tariffs offer limited rate stability through term plans, these require competitive carriers to agree to “lock-up” provisions, “take or pay” requirements, and shortfall penalties that themselves foreclose competition on the merits with the incumbent.

Further, a regime in which the Commission must assess the viability of landline services that depend on tariffed special access services simply is not workable. There is compelling evidence that incumbents have exploited their above-cost access rates to effect price squeezes that foreclose competition for a range of local services already, and the incumbents have the ability and incentive to do so for all their services in the future. Any attempt to assess whether and to what extent price squeezes will exist would pose insuperable “administrability problems” for the Commission. At at minimum, the Commission would then be required to determine (and to monitor) not only (i) the special access rates that incumbents unilaterally impose in the future and the quality of their tariffed services, but also (ii) the retail rates that they will charge and (iii) the retail-wholesale margin required to cover the other costs that efficient carriers would incur in providing finished services to retail customers. In this regard, it is precisely because of the complexity and unreliability of these determinations that Congress elected *not* to relegate competitive carriers to tariffed services and provided for UNEs instead.

For these reasons, *USTA II* did not even mention special access as a reason for remanding the *Triennial Review Order*’s rules allowing unbundled transport to be used in providing local landline services. *USTA II*, 359 F.3d at 574-75. At the same time, the Court stated that special access had to be considered in making impairment determinations for long distance services,

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because these services (like wireless services) are provided in a market that has been “robust[ly]” competitive. *Id.* at 592-93. But the long distance market is fundamentally different from the wireless market. CMRS firms have a long history of using special access to provide profitable service in competition with the Bells, and the structure of this market is such that incumbents have little or no ability to effect competitively significant price squeezes.

In sharp contrast, the Bells had been excluded from long distance markets for the past two decades precisely because they otherwise would have had the ability and incentive to use their control over last mile facilities and tariffed special access services to foreclose long distance competition. The provision of enterprise long distance services then became competitive *only* because the Bells were excluded and because all market participants thus were guaranteed that they would obtain high capacity transmission upon equal terms and at the same costs as did all their competitors. But with the Bells’ entry into long distance markets, that has all changed. Unless cost-based access is now provided to the high capacity loops and transport that cannot be economically obtained from other sources, competition will be impaired for all landline services, local and long distance alike.

Use Restrictions And Eligibility Criteria. For these same reasons, the time has come for the Commission to finally end the “use restrictions” or “eligibility” criteria that prohibit competitive carriers from using cost-based EELs to provide long distance services and even certain local services. The *Triennial Review Order* justified these restrictions on the ground that long distance services do not “qualify” for UNEs, but *USTA II* reversed that decision, holding that the eligibility restrictions must be eliminated unless the Commission finds that competitive carriers’ ability to offer long distance service will not be impaired if they are denied access to UNEs and relegated to special access services. But for the reasons just stated, it is impossible to

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make any such finding now that Bells have obtained full § 271 relief and have begun providing long distance services to enterprise customers nationwide.

Simply eliminating use restrictions, however, is insufficient to level the competitive playing field. The Bells have for years taken anticompetitive advantage of the inability of competitive carriers' to obtain access to loop and dedicated transport UNEs and the requirement that they purchase special access. The Bells forced competitive carriers to agree to onerous "lock-up" terms that require them to deal exclusively with the Bells. These provisions have one obvious intent and effect: to starve competitive carriers of the traffic they need to deploy or otherwise use bypass facilities. This in turn allows the Bells to keep demand on their network while also charging competitors (and end users) supracompetitive rates. The Commission should declare these tariff provisions unlawful and provide a "fresh look" to allow carriers to conduct negotiations in which they have true alternatives to Bell special access services.

Bulk Hot Cut Process. Facilities-based mass-market competition requires more than simply allowing competitive carriers the right to access unbundled loops. This right is meaningless unless there is an efficient process for disconnecting loops from an incumbent's switch and reconnecting them to the competitive carrier's switch. The Commission should therefore require incumbents to provide cost-based bulk hot cuts that satisfy specified performance standards. Absent such standards, competition for customers served by voice grade loops is impossible.

Other Issues Raised In Pending Proceedings. AT&T's comments also address the questions posed in the *Notice* concerning a number of other potentially related proceedings and issues. First, AT&T shows that state commissions have broad authority to maintain pro-competitive unbundling obligations even where the Commission declines to order unbundling

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under § 251. Second, AT&T shows that the Bells' § 271 unbundling obligations must be reflected in interconnection agreements and that such obligations are enforced by state commissions, which have primary authority to set the rates, terms and conditions of those obligations. Third, AT&T shows that the Commission lacks authority to override change of law procedures set forth in interconnection agreements.

Transition Rules. Finally, the Commission should rely on its express authority under § 251(d)(2) and its inherent authority to issue reasonable transition rules. Carriers have made considerable investments and formed business plans in reliance on the Commission's rules. Flash-cut elimination of UNEs would strand that investment and lead to potentially massive service interruptions. The Commission should thus adopt transition rules that phase out any "de-listed" UNEs over a two-year period.

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TABLE OF AT&T DECLARATIONS CITED IN COMMENTS

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A.	Beemon
B.	Benway, Holleron, King, Leshner, Mullan & Swift
C.	D’Apolito & Stanley
D.	Fea & Giovannucci
E.	Lieberman & Panereli
F.	Selwyn
G.	Sczepanski, Van de Water & Norris
H.	Stith

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TABLE OF FCC ORDERS CITED IN COMMENTS

<i>Access Reform Order</i>	First Report And Order, <i>Access Charge Reform et. al.</i> , 12 FCC Rcd. 15982 (1997)
<i>Amendment of Section 64.702 Order</i>	Memorandum Opinion and Order on Further Reconsideration, <i>Amendment of Section 64.702 of the Commission's Rules and Regulations</i> , 88 F.C.C. 2d 512 (1981).
<i>Bell Atlantic-NYNEX Merger Order</i>	Memorandum Opinion And Order, <i>Applications Of NYNEX Corp., Transferor, And Bell Atlantic Corp., Transferee, For Consent To Transfer Control Of NYNEX Corp., And Its Subsidiaries</i> , 12 FCC Rcd. 19985 (1997)
<i>Bell Atlantic/GTE Merger Order</i>	Memorandum Opinion And Order, <i>Application Of GTE Corp., Transferor, And Bell Atlantic Corp., Transferee For Consent to Transfer Control of Domestic and International Sections 214 and 310 Authorizations and Application to Transfer Control of a Submarine Cable Landing License</i> , 15 FCC Rcd. 14032 (2000)
<i>California 271 Order</i>	Memorandum Opinion and Order, <i>In the Matter of Application by SBC Communications, Inc, Pacific Bell Telephone Co., & Southwestern Bell Telecommunications Servs., Inc. for Authorization to Provide In-Region Interlata Services in California</i> , 17 FCC Rcd. 25650 (2002)
<i>CALLS Order</i>	Sixth Report And Order, <i>Access Charge Reform</i> , 15 FCC Rcd. 12962 (2000)
<i>CLEC Access Charge Reform Order</i>	Seventh Report and Order, <i>In the Matter of Access Charge Reform</i> , 16 FCC Rcd. 9923 (2001)
<i>Carrier Identification Codes Recon Order</i>	Order on Reconsideration, <i>Administration of the North American Numbering Plan, Carrier Identification Codes</i> , 12 FCC Rcd. 17876 (1997);
<i>First Application of Ameritech Michigan</i>	Order, <i>In The Matter Of Application By Ameritech Michigan Pursuant To Section 271 Of The Communications Act Of 1934, As Amended, To Provide In-Region, InterLATA Services In Michigan</i> , 12 FCC Rcd. 3309 (1997)
<i>Fourth Transport Rate Order</i>	Fourth Memorandum Opinion and Order on Reconsideration, <i>Transport Rate Structure and Pricing</i> , 10 FCC Rcd. 12979 (1995)
<i>Interim Order</i>	Order and Notice of Proposed Rulemaking, <i>Unbundled Access to Network Elements</i> , FCC 04-179 (Aug. 20, 2004).

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<i>ITTA Forbearance Order</i>	Third Memorandum Opinion and Order, Petition for Forbearance of the Independent Telephone & Telecommunications Alliance, 14 FCC Rcd. 10816 (1999)
<i>LEC Classification Order</i>	Second Report and Order, <i>Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LECs Local Exchange Area</i> , 12 FCC Rcd. 15756 (1997)
<i>ISP Intercarrier Compensation Order</i>	Order on Remand and Report and Order, <i>Intercarrier Compensation for ISP-Bound Traffic</i> , 16 FCC Rcd. 9151 (2001)
<i>Line Sharing Order</i>	Third Report And Order, <i>Deployment of Wireline Services Offering Advanced Telecommunications Capability</i> , 14 FCC Rcd. 20912 (1999)
<i>Local Competition Order</i>	First Report And Order, <i>Implementation Of The Local Competition Provisions Of The Telecommunications Act Of 1996</i> , 11 FCC Rcd. 15499 (1996)
<i>MCI-BT Merger Order</i>	Memorandum Opinion and Order, <i>Merger of MCI Communications Corporation and British Telecommunications PLC</i> , 12 FCC Rcd. 15351, (1997)
<i>MCI-WorldCom Merger Order</i>	Memorandum Opinion and Order, <i>Application of Worldcom, Inc. and MCI Communications Corporation for Transfer of Control of MCI Communications Corporation to Worldcom, Inc.</i> , 13 FCC Rcd. 18025 (1998)
<i>Michigan 271 Order</i>	Memorandum Opinion And Order, <i>Application Of Ameritech Michigan Pursuant To Section 271 Of The Communications Act Of 1934, As Amended, To Provide In-Region, InterLATA Services In Michigan</i> , 12 FCC Rcd. 20543 (1997)
<i>Non-Accounting Safeguards Order</i>	First Report and Order and Further Notice of Proposed Rulemaking, <i>Implementation of the Non-Accounting Safeguards of Sections 271 and 271 of the Communications Act of 1934 As Amended</i> , 11 FCC Rcd. 21905 (1996)
<i>OI&M Order</i>	Report and Order, <i>In the Matters of Section 272(b)(1)'s "Operate Independently" Requirement for Section 272 Affiliates</i> , 19 FCC Rcd. 5102 (2004)
<i>Pricing Flexibility Order</i>	Fifth Report And Order And Further Notice Of Proposed Rulemaking, <i>Access Charge Reform, Price Cap Performance Review For Local Exchange Carriers</i> , 14 FCC Rcd. 14221 (1999)

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<i>SBC/Ameritech Merger Order</i>	Memorandum Opinion And Order, <i>Applications Of Ameritech Corp., Transferor, And SBC Communications Inc., Transferee, For Consent To Transfer Control Of Corporations Holding Commission Licenses And Lines Pursuant To Sections 214 And 310(d) Of The Communications Act And Parts 5, 22, 24, 25, 63, 90, 95 and 101 Of The Commissions' Rules</i> , 14 FCC Rcd. 14712 (1999)
<i>SBC/Ameritech Merger Conditions Order</i>	Memorandum Opinion and Order, <i>Applications of Ameritech Corp., Transferor, & SBC Communications, Inc., Transferee</i> , 17 FCC Rcd. 19595 (2002)
<i>SBC Shared Transport NAL</i>	Forfeiture Order, <i>SBC Communications, Inc. – Apparent Liability for Forfeiture</i> , 17 FCC Rcd. 19923 (2002).
<i>Section 257 Report</i>	Report, <i>Section 257 Proceeding to Identify and Eliminate Market Entry Barriers for Small Business</i> , 12 FCC Rcd. 16802 (1997).
<i>Tariff 12 Order</i>	Order on Remand, <i>AT&T Communications, Revisions to Tariff F.C.C. No. 12</i> , 6 FCC Rcd. 7039 (1991)
<i>Tariff 15 Order</i>	Memorandum Opinion and Order, <i>AT&T Communications, Tariff F.C.C. No. 15</i> , 6 FCC Rcd. 5648 (1991)
<i>Texas 271 Order</i>	Memorandum Opinion And Order, <i>Application By SBC Communications Inc., Southwestern Bell Telephone Company, And Southwestern Bell Communications Services, Inc. d/b/a Southwestern Bell Long Distance, Pursuant To Section 271 Of The Telecommunications Act Of 1996 To Provide In-Region, InterLATA Services In Texas</i> , 15 FCC Rcd. 18354 (2000)
<i>Third Transport Rate Order</i>	Third Memorandum Opinion and Order on Reconsideration, <i>Transport, Rate Structure and Pricing</i> , 10 FCC Rcd. 3030 (1994)
<i>Triennial Review Order</i>	Report and Order on Remand and Further Notice of Proposed Rulemaking, <i>Review of Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers</i> , 18 FCC Rcd. 16978 (2004), as corrected by Errata, 18 FCC Rcd. 12020 (2004).

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<i>UNE Remand Order</i>	Third Report And Order And Further Notice Of Proposed Rulemaking, <i>Implementation of the Local Competition Provisions of the Telecommunications Act of 1996</i> , 15 FCC Rcd. 3696 (1999)
<i>Volume Discount Order</i>	Report and Order, <i>Private Line Rate Structure and Volume Discount Practices</i> , 97 F.C.C. 2d 923 (1984)

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of)	
)	
Unbundled Access to Network Elements)	WC Docket No. 04-313
)	
Review of the Section 251 Unbundling)	CC Docket No. 01-338
Obligations of Incumbent Local Exchange)	
Carriers)	
)	

COMMENTS OF AT&T CORP.

Pursuant to the Commission’s *Notice*, AT&T Corp. (“AT&T”) respectfully submits its comments concerning the availability of unbundled network elements under §§ 251(c)(3), 251(d)(2), and 271(c)(2)(B) of the Communications Act of 1934, as amended (the “Act”), 47 U.S.C. §§ 251(c)(3), 251(d)(2), 271(c)(2)(B).

ARGUMENT

I. THE COMMISSION’S FUNDAMENTAL CRITERIA FOR DETERMINING IMPAIRMENT AS APPLIED TO HIGH CAPACITY LOOPS AND TRANSPORT ARE PROPER AND SHOULD BE READOPTED ON REMAND.

It is a straightforward matter for the Commission to adopt rules for enterprise loops and dedicated transport that are “consistent with the U.S. Court of Appeals . . . decision” in *United States Telecom Ass’n v. FCC*, 359 F.3d 554 (D.C. Cir. 2004) (“*USTA II*”). *Interim Order* ¶ 1. *USTA II*’s grounds for remanding the *Triennial Review Order*’s rules for these elements were quite narrow. As AT&T demonstrates below, the Commission can readily satisfy these concerns and make national impairment findings for loops below 3 DS3s of capacity and for dedicated transport at or below 12 DS3s.

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Preliminarily, while it held that the Commission’s delegation to the states of the authority to grant exceptions to national impairment findings was unlawful, the Court did not find anything wrong with the *Triennial Review Order*’s national impairment findings for all DS1 loops, *Triennial Review Order* ¶¶ 325-27, and for DS3 loops with less than 3DS3s worth of capacity, *id.* ¶ 324. It thus rejected the Bells’ challenge to it.¹ Thus, although the Commission has decided to reconsider this finding and to assume, *arguendo*, that the national impairment finding for loops was vacated, *Interim Order* ¶ 9 n.29, that finding can readily be re-adopted, for the reasons explained below.

As to dedicated transport, after holding that the delegation to states of authority to make impairment determinations was unlawful, the Court concluded that the *Triennial Review Order*’s national impairment finding for dedicated transport at or below 12 DS3s could not stand independently after the “safety valve” of the state impairment proceedings was eliminated. The Court relied on the ground that the *Triennial Review Order*’s terms “suggested” that the

¹ In particular, after vacating the delegation to the states, the Court expressly limited its criticisms of the provisional national impairment finding to those involving the “unbundling of high-capacity dedicated transport facilities.” It discussed *only* the portions of the *Triennial Review Order* that pertained to dedicated transport and discussed none of the sections of the Order pertaining to loops. *USTA II*, 359 F.3d at 573-75. The Court then proceeded expressly to vacate the national impairment findings for dedicated transport and not to address the national impairment findings for loops. Because the Court expressly “denied” the petitions for review except to the extent that they were specifically granted, *id.* at 573-75, 594, *USTA II* thus upheld the Commission’s national impairment findings for high-capacity loops.

The point is confirmed by other aspects of the *USTA II* opinion. For example, the Court expressly relied on the Commission’s findings that because DS_n “loop alternatives” would be available as UNEs, there were “substitutes” that ameliorated the impairment faced by competitive carriers that are denied access to hybrid fiber copper loops. *Id.* at 582. This is further confirmation that the Court did not invalidate the national impairment findings for DS_n loops. If the Court had done so, it could not have upheld the Commission’s decision to eliminate unbundled hybrid loops on this ground. *Id.*

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Commission “doubt[ed]” that “a national impairment finding” could be made for all dedicated transport at or below 12 DS3s of capacity. *USTA II*, 359 F.3d at 574. In particular, the Commission had stated that the record was “insufficient[]” to make more granular determinations and had suggested that competitive alternatives may be available or economic on an indeterminate number of routes where the capacity thresholds were not met. *Id.* While the Court stated that “*some* over . . . inclusiveness” was an inevitable feature of unbundling rules, *id.* at 570 (emphasis added), and that the Commission had latitude to decline to engage in some inquiries on grounds of “administrabil[ity],” *id.* at 576, the Court held that there was no basis upon which it could uphold the rules. Given its vacatur of the delegation, the Court found that the *Triennial Review Order* had simply failed to undertake the inquiry necessary to determine that there generally are not alternatives for competitive carriers on routes below the established capacity thresholds, and the Commission also had not attempted to justify any overbreadth on administrability or other grounds. In addition, the Court faulted the dedicated transport rules on the grounds that the Commission had violated the Administrative Procedure Act (“APA”) by failing specifically and fully to address alternative market definitions and related claims that the Bells had advanced. *Id.* at 575.

Finally, the Court identified a separate and independent ground for vacating the *Triennial Review Order’s* grant of transport unbundled network element (“UNE”) rights to wireless carriers, despite the fact that transport is an incidental component of wireless networks and the success of wireless carriers over a 20 year period of providing wireless service by obtaining the incidental transport components under special access tariffs. *Id.* at 575-76. The Court held that the Commission’s rule categorically treating the availability of special access as irrelevant to impairment determinations had not been justified and could not support its decision to allow

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wireless carriers to purchase UNE transport. *Id.* At the same time, the Court did *not* state that the failure to consider special access had prejudiced the Commission's unbundling determinations governing the wireline local exchange and exchange access services that competitive carriers provide in competition with entrenched incumbent monopolists. In fact, the Court did not even discuss special access in the earlier sections of the opinion that addressed unbundling rights for these services. *Id.* at 574-75. Nonetheless, because the rule making special access irrelevant has been vacated generally, the Commission must consider the relevance of special access not only to the availability of UNEs for the wireless and long distance services that had historically been provided competitively through the use of special access, but also for wireline local services.

All of *USTA II*'s grounds for vacating the *Triennial Review Order*'s transport rules are easily answered in this remand – on grounds that are fully applicable to enterprise loops as well to transport.

First, the Court did not question the Commission's general impairment test. To the contrary, *USTA II* expressly approved the Commission's conclusion that the impairment inquiry should analyze whether there are entry barriers that mean that service would not likely be offered if competitive carriers were required to obtain facilities from sources other than the incumbent. As the Court stated, the Commission's "entry barrier" standard reasonably and plausibly addresses whether an element has "natural monopoly characteristics" or whether there are "first-mover advantages," "sunk costs," or "other structural impediments to competitive supply" that give incumbents "absolute cost disadvantages" over new entrants who rely on alternatives to the incumbents' facilities. *USTA II*, 359 F.3d at 571-72. Accordingly, the Commission should reaffirm that impairment is established by the presence of absolute cost disadvantages that stem

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from such structural impediments and that likely preclude the provision of service if cost-based access to incumbent LEC facilities is not available. While *USTA II* did question some aspects of the Commission’s impairment standard – whether entry barriers are evaluated on the basis of assuming there is an “efficient” or “inefficient” requesting carrier and its purported rule that state mandated cross-subsidies establish impairment in high-cost areas, *see id.* at 572-73 – these “failures to explain” can be easily addressed on remand and do not call into question the Commission’s core impairment test. *See infra* subpart A.

Second, *USTA II* did not question Commission’s conclusion that application of this impairment test to transmission facilities (*i.e.*, loops, transport, and entrance facilities) is most appropriately made on a capacity-specific basis. Nor could it. This principle flows directly from the indisputable fact that transmission facilities enjoy enormous scale economies, so that a competitive carrier’s ability to self-deploy depends critically on having demand that allows it to match the incumbent’s scale. At the same time, *USTA II* concluded that the *Triennial Review Order* had failed to turn “square corners” of administrative law in deciding that impairment determinations should be made on a route-specific and location-specific basis for transport and loops. While acknowledging that it “may be infeasible to define the barriers to entry in a manageable form” that may be applied to MSA or other broader market definitions, the Court faulted the Commission for “nowhere suggest[ing]” that it explored such alternatives or found them inferior to a route-by-route analysis due to higher “error costs” in terms of “false positives” and “false negatives” or otherwise. *Id.* at 574-75.

As detailed below, the evidence clearly shows that the Commission properly found that individual routes are the only correct market definitions for making impairment determinations regarding high capacity loop and transport facilities. Moreover, the evidence also clearly shows

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that the basic rule resulting from the Commission's route-specific analysis – *i.e.*, that each carrier is limited to a certain number of DS3s on any given point-to-point route – is both economically correct and extremely easy to administer. In this regard, data from the state impairment cases clearly demonstrate that such a test is much more highly predictive of impairment than a test that is applied across an MSA or some other large geographic area. *See infra* subpart B.

Third, there is no impediment to new national impairment findings for these elements. *USTA II* vacated the national findings for transport at or below 12 DS3s on a route only because the Commission in the *Triennial Review Order* had not found that there generally was impairment below this capacity threshold. To the contrary, because it did not then have sufficient evidence to make such granular determinations, the Commission did not deny that there might be substantial market-by-market variations, and the Commission suggested that there might be an indeterminate number of routes on which alternatives were in fact available to carriers who did not meet the 12 DS3 threshold for transport. And that, of course, is why the Commission had established triggers and the potential deployment standard for states to administer on a route-specific basis.

USTA II's vacatur of the national impairment findings thus rested solely on the ground that the Commission had made a national finding *without regard to* the presumed presence of significant market specific variations in competitive impairment – contrary to the D.C. Circuit's earlier holding in *USTA I*. By contrast, on the record that is now before the Commission – which includes the data from many state impairment cases – the Commission can readily find that it is in fact almost universally the case that transport alternatives are unavailable to competitive carriers at or below 12 DS3s, that loop alternatives are almost universally unavailable below 3 DS3s, and that administrability concerns justify whatever slight degree of overbreadth that may

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exist as a result of national impairment findings along these lines. The reality is that with the exception of a handful of extremely high density routes where transport is available at wholesale – which can either be treated as insufficient in number to justify an exception or dealt with through a summary certification process – the competitive deployment that has occurred is almost universally above the 12 DS3 level for transport and 3 DS3 level for loops, and any exceptions that exist rest on unique conditions from which no generalizations are possible. Further, there *also* is impairment in a vast range of circumstances in which competitive carriers actually *satisfy* these capacity thresholds. This further supports the Commission’s ability to ignore the handful of exceptions that may exist below the capacity thresholds. *See infra* subparts C & D.

Finally, because the issues raised by the availability of special access are relevant to use restrictions for EELs as well as to the impairment determinations for transport and loops, these issues are discussed separately in Parts III & IV. These sections explain that, just as *USTA II* suggested, there is no possible basis for the treating the availability of special access as a ground to deny competitive carriers access to loops and transport when the specific capacity thresholds that define impairment for each UNE is not reached and that there is no longer any basis to support any continuing use restrictions on EELs.

A. *USTA II* Did Not Disturb The Commission’s Core Impairment Test.

In *USTA I*, the Court faulted the Commission’s prior impairment test for failing to focus on cost disparities “linked” to the “natural monopoly” characteristics of the facilities at issue. 290 F.3d at 427. In the *Triennial Review Order*, the Commission responded directly to this criticism. In that *Order*, the Commission adopted a basic impairment test that considers whether scale economies, sunk costs, first mover advantages, absolute cost advantages and barriers within

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the control of the incumbent are likely to make entry uneconomic absent unbundling. *Triennial Review Order* ¶¶ 7, 87-91.

The Commission’s focus on the cost disadvantages not only was obviously correct, it was mandated both by basic economics and the Court’s ruling in *United States Telecom Ass’n v. FCC*, 290 F.3d 415, 426 (D.C. Cir. 2002) (“*USTA I*”), which held that “[a]ny cognizable competitive ‘impairment’ would necessarily be traceable to some kind of disparity in cost.” *USTA I*, 290 F.3d at 426. Where the incumbent enjoys a material cost advantage over competitors (and competitive carriers have no offsetting advantages), the incumbent can profitably set prices at a level that the competitor simply cannot match. *Triennial Review Order* ¶ 90 & n.302. This in turn deters (*i.e.*, serves as a barrier to) entry.

Barriers to entry unquestionably exist where – as is the case for transmission facilities – there is a combination of significant scale economies and sunk costs. *Id.* ¶¶ 87-88. The incumbent has already sunk its costs, while the would-be entrant has not. In this situation, there is the very real prospect that the incumbent will respond to entry by pricing all the way down to its short run marginal costs. The rational prospect that the incumbent will do this makes it less likely that an entrant can be profitable, and its entry will thus be deterred. *See id.* ¶ 88; *see also* Robert D. Willig, Determining “Impairment” using the Horizontal Merger Guidelines’ Entry Analysis at 3-4 (attached to *Ex Parte* Letter from C. Frederick Beckner III, AT&T, to Marlene Dortch (filed in CC Docket Nos. 01-338, Feb. 12, 2003)) (“Willig Letter”); *Ex Parte* Letter from Hon. Robert Bork, AT&T, to Chairman Michael Powell (CC Docket Nos. 01-338, Jan. 10, 2003), at 4-5 (“Bork Letter”). This is particularly true where, as with transmission facilities, the service at issue is characterized by steep scale economies and the incumbent serves virtually the entire market. *Triennial Review Order* ¶ 88 & nn.287-288. In that case, an entrant must deploy

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substantial capacity in order to achieve a cost structure comparable to the incumbent. But entry on such a massive scale will flood the market with excess capacity, making it unlikely that the entrant will be able to sell services at a price that will allow it to recover its sunk investment. Willig Letter at 3-4; Bork Letter at 4-5. Knowing this to be the case *ex ante*, the entrant will be deterred from entering and sinking its costs.

The critical point here is that, because of these basic economic considerations, a potential entrant understands that the price that currently exists in the marketplace may not exist post-entry. Rather, where there are sunk costs and economies of scale and scope, the incumbent will rationally be driven to price at a level that can prevent the entrant from recovering its sunk costs. It is the prospect of this rational economic behavior that deters the entry from happening at all. The Commission itself has recognized precisely this point:

If entry into an industry requires large sunk costs, the firm that incurs these sunk costs first (the incumbent) can have a tremendous advantage. Potential new entrants may realize that any large scale facilities-based entry into the market will probably force prices to decrease and those prices may be in fact below the point necessary to recover the sunk cost investment. As a result, facilities-based entry will be deterred.

Section 257 Report ¶ 18 n.48. *See also MCI-BT Merger Order* ¶ 162 (same).

In their challenge to the Commission’s unbundling rules in *USTA II*, the Bells contended that the Commission’s impairment standard was “so open-ended that it imposes no meaningful constraints on unbundling, and would be unlawful even if applied by the FCC itself.” *USTA II*, 359 F.3d at 571. The Court, however, largely rejected this criticism, holding that the “[o]rder’s interpretation of impairment is an improvement over the Commission’s past efforts in that, for the most part, the Commission explicitly and plausibly connects factors to consider in the impairment inquiry to natural monopoly characteristics . . . or at least connects them (in logic

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that the ILECs do not seem to contest) to other structural impediments to competitive supply.”
Id. at 571-72.

The Court also noted, however, that there was “one important respect” in which the Commission’s impairment test appeared to lack sufficient content. *Id.* at 572. It stated that while the Commission’s impairment test properly looked to see whether these cost disadvantages rendered entry uneconomic, it did not expressly answer the question of “[u]neconomic by whom?” *Id.* Believing that any number of standards could be imagined (*e.g.*, the “most efficient CLEC,” an “inefficient” CLEC, “an ‘average’ or ‘representative’ CLEC”), the Court directed the Commission to clarify this issue on remand so as to ensure that its impairment test was not “too open-ended” to allow consistent implementation. *Id.*

The Court’s concern is easily answered. The *Triennial Review Order* required that impairment determinations be based on the alternatives available to efficient competitive carriers using the most efficient technology, and is the test that should be applied in this remand. Indeed, this standard was implicit in the *Triennial Review Order*’s impairment standard, for determinations as to whether there are entry barriers inherently focus on efficient carriers. And it was also inherent in the test that the Commission applied in determining that competitive carriers cannot economically provision loops and transport unless they have capacity that exceeds the thresholds of 2 DS3s and 12 DS3s. Further, the *Triennial Review Order* elsewhere expressly required that this test be applied by others making impairment determinations for individual elements. Specifically, in discussing the application of its impairment standard by state commissions, the Commission stated that its impairment standard requires a determination of “whether entry is likely to be economic utilizing the most efficient network architecture available to an entrant.” *Triennial Review Order* ¶ 517. The Commission further added that “[s]tate

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commissions should determine if entry is economic by conducting a business case for an *efficient* entrant.” *Id.* n.1579 (emphasis added); *see also id.* ¶ 115 (standard does not focus on business strategies of particular competitive carriers that could reward inefficient entrants). Use of such an “efficient CLEC” standard makes obvious sense, for the purpose of the Act is to induce efficient entry, exit and expansion decisions. Thus, to the extent that a competitive carrier is unable to self-provide a facility only because it is inefficient, unbundling should not be required. Conversely, however, where duplication of a facility by a competitive carrier is inefficient and where there are no efficient alternatives to the incumbent’s network, unbundling of the network element must be required.

Finally, *USTA II* also criticized one other aspect of the *Triennial Review Order*’s impairment standard: its purported conclusion that impairment exists in any high-cost areas where rates are held below cost by state commissions in order to promote “universal service.” 359 F.3d at 573. The Court stated that any such rule would be inconsistent with the holding of *USTA I* that impairment determinations must be based on “structural features that make competitive supply wasteful.” *Id.* It also stated that the purported *Triennial Review Order* rule could not be defended on the ground that the rule would not lead to entry in any of these areas, and the Court identified conditions in which such entry might occur. *Id.*

The primary significance of this issue applies to mass market switching and UNE-P, and it has little or no importance for high capacity loops and transport. As a threshold matter, the Commission has never considered special access to be a source of implicit universal service subsidies. To the contrary, the Commission’s “established practice” is that “special access will *not* subsidize other services.” *See, e.g., Access Reform Order* ¶ 404; *see also UNE Remand Order* ¶ 496 n.994 (in its universal service proceeding, the Commission “did not propose to treat

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special access services as if the current prices of those services included implicit support for universal service”).

Moreover, the Commission removed *all* implicit subsidies from interstate access charges in the *CALLS Order*; thus, the Bells can no longer claim that the availability of unbundled loop-transport combinations will erode universal service subsidies by causing migration from switched access. In that order, the Commission found that “at this time \$650 million is a reasonable estimate of the amount of universal service support that currently is in our interstate access charge regime.” *CALLS Order* ¶ 202. Accordingly, the Commission removed \$650 million from interstate access charges and replaced it with an explicit \$650 million universal service fund. *See id.* ¶¶ 195, 201. The Commission expressly found that the \$650 million fund would be fully “sufficient to keep [local] rates affordable and reasonably comparable” during the life of the CALLS Plan, and that no additional subsidies from interstate access charges would be necessary. *Id.* ¶ 201. The Commission concluded that the \$650 million “estimate should be reevaluated at the end of the five-year plan to determine the sufficiency of the fund based on the development of competition and market-based pricing.” *Id.* ¶ 203. With the adoption of the CALLS Plan, the Bells have no conceivable claim that inflated special access rates are necessary to protect universal service subsidies.

However, to the extent the issue has any pertinence at all to these UNEs, the short and obvious response is for the Commission now to make explicit that impairment can only be found where there are structural impediments that mean that competitive supply of a facility by a competitive carrier will not occur in a particular market – irrespective of whether the prevailing retail rates that the incumbent is permitted to charge are above-cost or below-cost. This is a

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determination that the Commission can readily make for high capacity loops and transport below the specified capacity thresholds.

B. The Commission Should Continue To Apply A Capacity-, Location- And Route-Specific Market Analysis In Making Impairment Determinations for High Capacity Loops and Transport.

In the *Triennial Review Order*, the Commission applied two analytic principles in making impairment determinations for high capacity transmission facilities. First, it held that loop and transport impairment should be determined on a capacity-specific basis. Second, it held that loop and transport impairment should be determined on a location- and route-specific basis. The first consideration was not disturbed at all by *USTA II*. And while *USTA II* concluded that the Commission had not fully justified all aspects of its decision to treat routes as relevant markets, the Commission can readily do so now.

1. The USTA II Decision Did Not Disturb The Commission’s Finding That Loop And Transport Impairment Should Be Determined At A Carrier-Specific And Capacity-Specific Level.

The *Triennial Review Order* properly organized its analysis “based on capacity level because it is a more reliable indicator of the economic abilities of a requesting carrier to utilize third-party alternatives, or to self-deploy.” *Triennial Review Order* ¶ 376. This finding is well grounded in the basic economics of the deployment of transmission facilities. Fea-Giovannucci Dec. ¶ 25-30. As the Commission found (*Triennial Review Order* ¶¶ 303, 370-71), and as described in greater detail in Part II *infra*, loops and transport enjoy strong natural monopoly characteristics. They are characterized by enormous fixed costs that do not vary with capacity. Moreover, incumbents have already built ubiquitous facilities designed to serve the entire market. Thus, they can spread the enormous fixed costs of those facilities over many customers (including both mass market and enterprise-level customers), thereby achieving extremely low per-unit costs. Competitive carriers, in contrast, face the entry barrier of replicating ubiquitous

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sunk facilities that are characterized by enormous economies of scale. And if they cannot obtain access to those facilities at cost-based rates, they face significant absolute cost disadvantages compared to the incumbent – and real and potential price squeezes – in attempting to provide any service that relies on such facilities. *See infra* Part III.

For these reasons, the ability to self-deploy correlates strongly and directly with the *capacity* of the facility at issue. Fea-Giovannucci Dec. ¶ 33-36. A competitive carrier can match the incumbent’s cost structure only on individual routes where the competitor itself can serve very high demand, thereby allowing the competitive carrier to achieve per-unit costs close to those of the incumbent. *Id.* ¶ 30. Whether any particular carrier can deploy its own transmission facilities is thus a function of whether *that individual carrier* has enough traffic *on a given route* to justify the investment of the enormous fixed costs necessary to construct a *specific* new transmission facility. *Triennial Review Order* ¶ 377 (“[b]ecause a carrier using higher capacity levels of transport has a greater incentive and broader revenue base to support the self-provisioning of transport facilities, we adopt an approach to analyzing transport that considers different capacity levels”). These facts also mean that the relevant inquiry must be carrier specific: the fact that one carrier may have sufficient demand on a route to justify deployment does not, of course, mean that any other carriers have similar demand.

The Court in *USTA II* did not at all question the Commission’s finding that impairment differs according to the capacity of a transmission facility and did not invalidate the Commission’s use of a carrier-specific, capacity-specific test. Indeed, this is just the type of “nuanced” analysis that the Court demanded. *USTA II*, 359 F.3d at 563. Moreover, as explained in greater detail below, the engineering and economic evidence sponsored by AT&T herein confirms that a carrier’s ability to self-deploy transmission facilities correlates very strongly with

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the capacity it will provide (and thus the revenues or other cash benefits it could obtain from those facilities). Indeed, the Bells' own testimony provides conclusive evidence that self-deployment of loops is not economically feasible below 3 DS3s of capacity and that self-deployment of transport is not economically feasible below 13 DS3s of capacity. *See infra* Part II.C. The Commission should thus again make impairment determinations on a capacity-specific basis.

2. The Relevant Market for High Capacity Facilities is Point-to-Point Routes and The Commission Should Expressly Reject the Proposals To Use MSAs Or Other Markets.

The D.C. Circuit understood the economic factors that compel treating point-to-point routes as the relevant markets for these impairment determinations and expressly stated that “it may be infeasible” to define entry barriers applicable to transmission facilities in a way that would allow the concept to be applied to MSAs or the other markets that incumbents had previously advocated. *USTA II*, 359 F.3d at 575. Nonetheless, *USTA II* held that the *Triennial Review Order's* treatment of the issue was insufficient to satisfy the stringent standards of decisionmaking imposed by the APA, concluding that the Commission had not expressly explored the incumbents' proposed alternatives and had not expressly found MSAs and other such markets to be inferior to the Commission's route-by-route analysis. Thus, the Court indicated that the Commission must address whether a route-by-route analysis represents the best means of identifying impairment and that it should consider whether MSAs or other possible geographic markets would have higher “error costs” in terms of “false positives” and “false negatives.” *Id.* at 574-75.

The simple answer to the Court's concerns is that the Commission has considered the alternatives and has in fact identified the most appropriate analysis to measure impairment for loops and transport. A route-by-route analysis is the economically correct way to proceed; it is

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the rule with the lowest “error costs,” and it is extremely easy to administer in the conditions that prevail today.²

As a threshold matter, this issue really is not in dispute at all. High capacity loops and transport can be provided either as UNEs or as special access services. But regardless of the form in which they are provided, the Commission has consistently held that high capacity loops and dedicated transport are provided in “point-to-point markets” or markets of “discrete local areas.” See *MCI-WorldCom Merger Order* ¶ 166; *LEC Classification Order* ¶ 67; *Bell Atlantic-NYNEX Merger Order* ¶¶ 54-56. And critically, the Bells’ own economists have repeatedly argued that, “the [special access] services in question are point-to-point connections, and a point-to-point connection cannot be transported from other parts of the region.” Affidavit of Karl McDermott and William E. Taylor, CC Docket No. 99-24, at 6-7 (filed Jan. 20, 1999); see also Reply Comments of Qwest, Farrell Reply Dec. ¶ 29 (filed in CC Docket 01-338, July 17, 2002) (“Given its point-to-point nature, one would expect that dedicated transport would require more of a geographically-focused inquiry”); Reply Comments of BellSouth, Harris Reply Dec. ¶ 6 (filed in CC Docket No. 01-337, Apr. 22, 2002) (“The geographic scope of the market for broadband access is local”); Comments of Verizon, Declaration of Alfred Kahn and William Taylor at 25 (filed in RM No. 10593, Dec. 22, 2002) (special access facilities are “point-to-point”).

The economic factors that underlie the impairment inquiry are likewise route-specific. As explained above, any particular carrier’s ability to deploy its own transmission facilities is a function of whether that specific carrier has enough traffic on a given route to justify the sunk

² AT&T explains the basis for the particular capacity thresholds that should determine when a transmission facility can reasonably be self-deployed *infra* in Part II.

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investment of the enormous fixed costs necessary to construct a facility. This point is so incontestable that the Bells themselves have conceded it. *See* SBC Reply at 148 (filed in CC Docket 01-338, July 17, 2002) (“As the Commission has recognized, transport is a point-to-point facility. It is accordingly efficiently deployed [only] where there is *sufficient volume* between the relevant points.”) (emphasis added).

Accordingly, the Commission should now clarify that its *Triennial Review Order* rules did not – and its Order on Remand will not – “ignore facilities deployment along similar routes when assessing impairment.” *Compare USTA II*, 359 F.3d at 575. The Commission can and should clarify that such evidence is not irrelevant, and that it has considered any such circumstances in determining that impairment exists below the capacity thresholds. In particular, as discussed above, the capacity test determines the routes on which deployment of alternative facilities is and is not economic, and thus determines what routes are and are not “similarly situated” in terms of the entry barriers that a competitive carrier faces. If points A, B, and C are all in the same geographic market and carriers are “similarly situated” with regard to the supply-side and demand-side barriers to entry that the Commission says are “controlling,” *compare id.*, it *must* mean that that those carriers have comparable capacity needs on each route. Because capacity needs determine whether the scale economies and sunk cost entry barriers can be overcome, carriers cannot be “similarly situated” with respect to the entry barriers that are controlling unless their capacity needs are the same on those routes.

Similarly, while not irrelevant, the mere existence of standalone “low” capacity facilities on a particular route is not sufficient to establish that competition is likely on that or any other route with similar capacity. *See USTA II*, 359 F.3d at 575 (upholding *Triennial Review Order*

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¶ 401). Here, the evidence shows that there has been only *de minimis* deployment before the 2 DS3 and 12 DS3 capacity thresholds. *See* Part II.B.

Further, the evidence shows that that where such deployment has occurred, it was uneconomic and in no way indicates that alternatives would exist on other routes where the capacity thresholds are not met. Specifically, some carriers in the past deployed facilities on routes that turned out to have insufficient capacity to support them – based on a “build it and they will come” strategy or other miscalculations or predictions that turned sour. *See* Fea-Giovannucci Dec. ¶ 31. This experience showed that a “build it and they will come” strategy can be (and often is) a recipe for disaster in light of the sunk nature of transmission investment, for if the necessary traffic volumes do not materialize, the investment will be stranded. *Id.*; *see also* Willig Letter at 4; Bork Letter at 4-5. And that is exactly what happened. Many of carriers that attempted this entry strategy were never able to attract the capacity to make their investment profitable and went bankrupt. Selwyn Dec. ¶¶ 21, 30-31. No rational carrier would deploy facilities on that or any other routes with similar capacity levels today, D’Apolito-Stanley Dec. ¶¶ 12-24, and the existence of *uneconomic* facilities on one route cannot support an impairment finding on a route with the same capacity.

These basic economic facts provide ample basis for the Commission to re-adopt its prior findings that impairment should be determined on a *route*-specific and *carrier*-specific basis. The mere fact that one carrier has amassed enough traffic on a given route does not mean that other carriers, who do not have that much traffic, could also build their own facilities on that route. Similarly, the mere fact that one carrier has obtained enough traffic to deploy facilities on one route does not mean that that same carrier could build a facility on a nearby route, where it does not have enough traffic. Moreover, as also shown below, *see infra*, because the cost of

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constructing the infrastructure is so high, even small differences in the length of the facilities needed to provide traffic on a route can make a huge difference in whether a carrier is able to afford the construction costs.

A route-specific analysis is also the only type of analysis that can account appropriately for non-operational impairment factors. As the Commission expressly recognized in the *Triennial Review Order*, and as explained in greater detail in Part II, there is a wide a range of circumstances in which competitive carriers could satisfy these capacity thresholds (*i.e.*, where self-deployment is economically viable), but in which other operational entry barriers would prevent them from offering service unless high capacity loops and transport are available as UNEs. For example, competitive carriers are often unable to deploy transmission facilities because of the inability to secure the necessary rights-of-way from municipalities or building access from landlords. *Triennial Review Order* ¶¶ 303, 305, 371. These operational factors “decisively” establish impairment, *USTA II*, 359 F.3d at 570, and they can meaningfully analyzed only on a route-specific basis.

For all these reasons, it would produce substantial errors simply to assume that deployment by one carrier on one route means that deployment is feasible by other carriers on other routes and that there is no impairment absent UNEs on those other routes. That would be a “false negative,” to use *USTA II*’s phrase, because it would predict *non*-impairment when in fact competitors are actually impaired.

For the same reason, treating MSAs as the relevant market and making findings of MSA-wide non-impairment based on the existence of competitive deployment merely on *some* dense routes in an MSA – as the incumbents urge – would produce far greater errors. The result would be enormous amounts of “false negatives” – *i.e.*, erroneous findings of non-impairment – on

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routes in the MSA where capacity thresholds have not been met and where deployment is uneconomic. The reasons are explained in more detail in Part II, *infra*. The reality is that even in MSAs where there is some minor evidence of competitive wholesaling on certain routes, there are few (and often no) DS1, DS3, or dark fiber alternatives for competitive carriers on other routes. In *USTA II*'s words, it would thus be wholly “infeasible” to make entry barrier determinations in a “manageable form” if the MSAs were deemed to be the relevant market for making impairment determinations for loops and transport. Beyond that, the result would be extraordinarily high levels of “false negatives” because nonimpairment would be found on multiple routes where impairment exists.

This is true even if the incumbent has satisfied the Commission’s “triggers” for special access pricing flexibility. As the Commission explained, “competition in some parts of a market may be sufficient to constrain prices, but insufficient to demonstrate a lack of impairment.” *Triennial Review Order* ¶ 104. For example, with respect to loops, the Commission observed that “[i]ncumbent LECs have received special access pricing flexibility in numerous MSAs throughout their regions, based almost exclusively on meeting the *Pricing Flexibility Order*’s triggers based on special access revenues,” but “the special access revenue triggers require only a single collocated competitor to purchase substantial amounts of special access in a concentrated area.” *Id.* ¶ 341. Thus, “this test provides little, if any, indication that even that competitor has been able to widely, if at all, self-deploy alternative loop facilities in that area. Evidence of self-deployment of transport facilities is not necessarily evidence of the economic ability of a competitive LEC to self-deploy loops.” Moreover, “the presence of a single competitive LEC’s collocated transport facility as a trigger for purposes of protecting consumers from anticompetitive pricing, *i.e.*, the purpose of our pricing flexibility rules, is not sufficient evidence

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that facilities-based competitive entry into a market at the local loop level is economically feasible.” *Id.* Finally, the Commission emphasized that using an MSA-wide “market” would generate substantial “false negatives” because “the record simply does not contain evidence that loop impairment/non-impairment determinations can be appropriately made on a zone basis *due to the location-specific factors which impact impairment determinations* at most high-capacity loop levels.” *Id.* ¶ 341 (emphasis added).

These points are illustrated by the arguments that the incumbents have made in *ex parte* filings since *USTA II* was decided. *See, e.g., Ex Parte* Letter from Michael Glover, Verizon, to Marlene Dortch, Att. at 20 (filed in CC Docket No. 01-338, July 2, 2004) (“7/2/04 Verizon Letter”). While the incumbents here persist in arguing that MSAs should be the relevant market for making impairment determinations, the only way that they can make this argument is by assuming away the whole impairment inquiry. They assume that competitive carriers can self-provision their own loop and transport facilities on virtually all the routes in the largest MSAs and can economically provide service on the few remaining routes using special access. *Id.* Thus, the incumbents have tacitly acknowledged that impairment determinations must be made on a route specific basis and have justified their proposed “market” only by assuming (or asserting) that there is no impairment on individual routes throughout larger MSAs, either due to the purported economic feasibility of self-supply or the assured adequacy of special access. But because the Commission must make “nuanced” determinations of where there is and is not impairment – and cannot assume this core issue away – the incumbents’ own filings confirm that the relevant markets for these determinations are the individual routes between pairs of an incumbent LEC’s wire centers. It is only at that level that it is feasible to determine whether there are barriers to entry that preclude competitive deployment and whether the existence of

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special access affords grounds to eliminate unbundling where impairment otherwise exists. Thus, when impairment has to be assessed – as it does here – the *USTA II* Court correctly surmised that it is “infeasible to define the barriers to entry in a manageable form” and “usefully” to apply the impairment standard “to MSAs (or other [such] markets).” 359 F.3d at 575.³

C. There Is No Impediment To Nationwide Impairment Findings For High Capacity Loops And Transport.

There is nothing in *USTA I* or *USTA II* that stands in the way of the Commission’s ability to make national findings of impairment for loops and transport below the specified capacity thresholds. As more fully explained in Part II, *infra*, the data before the Commission – including the data gathered in connection with the state impairment cases – establishes that it is virtually always uneconomic for competitive carriers to deploy their own facilities if they do not have the traffic volumes identified in the capacity limits and that the deployment that has occurred is – with only trivial exceptions that rest on unique factors – by competitive carriers who *exceed* those traffic volumes on particular point-to-point routes. Given that these data were collected in a wide variety of states of different geographic and demographic profiles, there is no basis in the record for the Commission to conclude that these conditions do not apply throughout the nation. Thus, there similarly is no basis for the Commission to find that there are significant market-by-market variations that would be inconsistent with an undifferentiated nationwide finding of impairment in these conditions.

³ Conversely, a decision to treat loop or transport markets as particular point-to-point routes will not itself produce substantial “false positives” – *i.e.*, findings of impairment in markets where there is none. If there were any risk of “false positives” here, it would not result from the definition of the relevant market as the individual route, but rather from the criteria that were adopted to define where impairment exists.

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In this regard, nothing in *USTA II* (or *USTA I*) bars national impairment findings in this circumstance. The Court recognized that national impairment findings for voice-grade copper loops were proper, for there generally is no deployment of alternative loops anywhere in the nation. 359 F.3d at 561. By contrast, it vacated the *Triennial Review Order*'s provisional impairment findings for dedicated transport only because the *Triennial Review Order* on its face made statements that established that the Commission had neither made sufficiently undifferentiated national impairment findings nor made any other legally sufficient attempt to justify a nationwide requirement that transport be made available below the identified capacity threshold.

In particular, the Commission did *not* find that competitive alternatives generally did not exist for competitive carriers who required fewer than 12 DS3s of capacity. To the contrary, as *USTA II* noted, the Commission stated that it had *insufficient evidence* to determine whether and to what extent there were markets where competitive carriers with lower traffic volumes had deployed or were using alternatives to incumbent LEC transport, and the Commission suggested to the Court that there could be an indeterminate number of such markets where competitive carriers would not be impaired without access to such facilities. 359 F.3d at 574. Responding to these statements, the Court concluded that the "Order itself suggests that the Commission *doubts* that a national impairment finding is justified on this record." *Id.* (emphasis added). Thus, the Court treated the *Triennial Review Order*'s delegation of market-by-market impairment inquiries to the states as an *admission* that the Commission had not conducted a sufficient inquiry to enable it to make an undifferentiated nationwide impairment determination for transport.

At the same time, the *Triennial Review Order* had not attempted to justify the potential overbreadth of its national finding on any other legally sufficient ground. The Court held that

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the delegation to the states was unlawful, and that because the Commission had relied solely on “impairment” – without invoking administrability concerns or the “at a minimum” clause of § 251(d)(2) – the Court had no occasion to consider whether and to what extent these concerns could justify the over-inclusiveness inherent in the *Triennial Review Order*’s provisional national impairment finding.

But given the evidence that is now available, there is no basis for the Commission, or a reviewing court, to conclude that there may be substantial deployment (or alternative supply) of high capacity loops or transport on routes where the capacity thresholds are not met. And the clear teaching of *USTA I* and *USTA II* is that, in the *absence* of evidence of *substantial* market specific variations in impairment, nationwide impairment findings that rest on evidence of national conditions are valid. The only situation when undifferentiated national findings are invalid is when there is “evidence that markets vary *decisively* (by reference to the impairment criteria).” 359 F.3d at 570 (emphasis added); *see also id.* (recognizing that “*some* over- . . . inclusiveness” is inevitable in national impairment findings). *USTA II* also recognized that “administrability” concerns can justify decisions by the Commission to decline to undertake complex factual inquiries that will inherently have little effect on the ultimate outcome.

On the record now before the Commission – which includes the data from the state impairment cases – the Commission can readily find that it is almost universally the case that transport alternatives are *not* available to competitive carriers at or below 12 DS3s, that loop alternatives are almost universally unavailable below 3 DS3s, and that administrability concerns justify whatever slight degree of overbreadth will exist as a result of national impairment findings along these lines. As explained more fully in Part II, *infra*, the microeconomic evidence demonstrates that these are the capacity levels at which competitive carriers have determined that

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it generally is economic for alternative facilities to be deployed – assuming other entry barriers are also overcome. Further, as detailed in Part II, *infra*, the reality is that, except for a handful of extremely high density routes where transport is available at wholesale – which can either be treated as insufficient in number to justify an exception or dealt with through a summary certification process – actual competitive deployment is almost universally above the 12 DS3 level for transport and the 2 DS3 level for loops, and any exceptions that exist rest on unique conditions from which no generalizations are possible.⁴ Thus, trying to identify these outliers would impose substantial burdens on the Commission and carriers without producing significant improvement in the accuracy of the Commission’s rules.

In this regard, the Commission is entitled to consider factors other than “impairment” in making unbundling determinations. The “at a minimum” clause of § 251(d)(2) authorizes the Commission to consider a range of other factors. For example, in *USTA I*, the Court expressly “assumed” that the “at a minimum” clause authorized the Commission to order unbundling in conditions when there is no impairment, holding only that the Commission’s “belief” in the benefits of the broadest possible unbundling was insufficient to justify the extreme overbreadth that was present in the particular rules that were there at issue. *USTA I*, 290 F.3d at 425. The capacity thresholds (and any self-executing wholesale trigger the Commission may choose to

⁴ Indeed, the evidence shows that a capacity- and route-specific rule is significantly *under inclusive* in identifying impairment, for there are many instances in which a carrier cannot build its own facilities even on routes where it has enough traffic to economically justify deployment. That is so because competitive carriers face a host of additional barriers to deployment beyond those associated with scale economies. These include the availability of access to rights of way, construction permits and buildings; the presence of unanticipated physical obstacles; the Bells’ inherent ability to provide service much more quickly; and the refusals of existing customers of competitive carriers to allow the competitive carrier to “roll” their circuits to the competitive carrier’s own facilities; and lock-in provisions of the Bells’ special access tariffs. *See infra*.

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adopt) plainly capture conditions in which alternatives to transport and loops are generally uneconomic. Thus, administrability concerns justify any slight over- or under-inclusiveness of the rules. That is especially so because the unbundling rules that the Commission adopts here – like all Commission rules, *see* 47 C.F.R. § 1.04 – are subject to waiver upon a showing that the generally applicable conditions that justify the national rule do not exist in certain individual respects. *ICORE, Inc. v. FCC*, 985 F.2d 1075, 1080 (D.C. Cir. 1993) (“a rule with a rational basis, yet otherwise impermissibly broad, ‘can be saved by the ‘safety valve’ of waiver or exemption procedures.’” (quoting *KCST-TV, Inc. v. FCC*, 699 F.2d 1185, 1200 (D.C.Cir.1983) (Scalia, J., dissenting)); *Alltel Corp. v. FCC*, 838 F.2d 551, 561 (D.C. Cir.1988) (same).

II. THE COMMISSION SHOULD RE-ADOPT RULES LIMITING REQUESTING CARRIERS TO 2 DS3S OF LOOPS AND 12 DS3S OF TRANSPORT WITHOUT ADDITIONAL TRIGGERS.

The evidence now available to the Commission shows – without the slightest doubt – that competitors cannot build their own facilities to provide service at or below the capacity thresholds established in the *Triennial Review Order*.⁵ This confirms more strongly than ever that the Commission’s original judgments in the *Triennial Review Order* regarding the point at which competitive carriers are not impaired for loops and transport were reasonable and that they may – and should – be retained under any reading of *USTA II*. Indeed, the new evidence submitted here by AT&T and by the Bells in recent *ex partes*, coupled with the extensive evidence collected in the state commission impairment proceedings, make it crystal clear that there are only a *de minimis* number of individual cases in which competitive carriers are not

⁵ In the *Triennial Review Order*, the Commission required unbundling for DS1 and dark fiber loops and for up to 2 DS3s of loop capacity per location (§ 324); the Commission’s rules also require unbundling of DS1 and dark fiber transport and up to 12 DS3s of transport on any route (§ 388).

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impaired without access to UNE loops and transport at the 2 DS3 and 12 DS3 capacity levels for loops and transport, respectively. Moreover, the evidence AT&T and other competitive carriers present here demonstrates that those thresholds are in fact significantly *over-predictive* of non-impairment and that there are a host of circumstances in which competitive carriers are impaired without access to UNE loops and transport at even higher capacities. Thus, on balance, even these capacity thresholds are more favorable to incumbents than to requesting carriers, and there is no need to establish further “triggers” to provide for even more de-listing.

First, as shown below, since 2003, AT&T has reviewed all of its internal business cases for loops and transport, and also provides a business case review applicable to new loop and transport construction. All of those data point to a single conclusion: prospective self-deployment of loops or transport is impossible to justify with the new revenues and cost savings from only 2 DS3s of traffic (for loops) or 12 DS3s of traffic (for transport) in all but the most extreme and exceedingly rare circumstances. *A fortiori*, the reasonably anticipated positive cash flow generated from only DS1 level traffic is also insufficient to support such construction.

The principal cost driver for both loop and transport construction is the extremely high cost of building new outside plant, which increases with the length of the transmission link. As the Commission has recognized, these costs are both fixed and largely sunk. *Triennial Review Order* ¶¶ 205, 371. Therefore, such construction is prohibitively expensive, unless a carrier can be assured that it will have a very large amount of committed capacity to carry over the new facilities. *Id.* ¶ 303. For this reason, the DS3 traffic thresholds set in the *Triennial Review Order* are actually very generous to the incumbents, because there are many circumstances in which a carrier would need considerably *more than* 2 or 12 DS3s to justify the cost of construction. And the Commission itself has recognized that there are other barriers, such as lack of access to rights

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of way, lack of building access, and customer refusals to sign releases for circuit rolls that often prevent construction even when the economics are otherwise favorable. *Triennial Review Order* ¶ 209. In addition, special access lock-in tariffs also act to preclude carriers from self-deploying their own facilities or leasing wholesale facilities of any capacity from third parties.

Accordingly, there is no need for the Commission to adopt any additional “triggers” that may further limit unbundling. Pursuant to the Commission’s request in the *Triennial Review Order*, many state commissions conducted extensive investigations into whether there are individual routes where there are multiple alternatives for DS1 or DS3 loops or transport. CompTel, ALTS and numerous competitive carriers sponsored a review of the evidence by QSI Consulting, Inc., for 14 state proceedings with the most complete factual records, including large states such as California, Florida, Texas and Illinois, and they have recently provided those data to the Commission.⁶ These data clearly demonstrate that there are proportionally very few routes or building locations where the Bells even challenged the Commission’s national impairment finding. But even more striking, there are virtually *no* legitimate exceptions to the Commission’s national determination.

The QSI Analysis shows that there are – collectively – only 130 buildings in 12 states where two or more competitors self-provide loops with less than 2 DS3s of capacity, and fewer than 50 buildings where wholesale DS3 or DS1 loops are available. Similarly, QSI’s analysis shows there are only a *total* of 55 transport routes in 14 states (including New York) with three or more self-providers of DS3 transport and fewer than 50 routes in those states where there are

⁶ Attachment to *Ex Parte* Letter from CompTel/Ascent, *et al.* to Marlene R. Dortch, FCC, dated October 4, 2004, “Analysis of State Specific Loop and Transport Data,” prepared by QSI Consulting, Inc. (“QSI Analysis”).

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two or more wholesalers of DS3 or DS1 transport. QSI Analysis at 2-3. Thus, it is clear that the capacity thresholds in the *Triennial Review Order* were exceedingly conservative and favorable to the incumbents, because they generate far more “false negatives” – *i.e.*, requirements of de-listing where there is in fact impairment – than “false positives” – *i.e.*, requirements of unbundling when there is no impairment. *See USTA II*, 359 F.3d at 575.

Under these circumstances, the Commission need not require any additional “granularity” in its impairment review, because the capacity thresholds – which are very easy to administer – so rarely identify cases in which there is actually “no impairment.” Indeed, given the fact that, as explained above, the capacity thresholds are actually over-inclusive in many situations – including the inability to obtain access to rights of way or building access, customer refusal to sign releases permitting rolls, ILEC lock-in special access tariffs, and other barriers – it would be inappropriate for the Commission to allow additional de-listing if it does not also allow carriers that remain impaired above the capacity limits to seek exceptions to the national rule.

Finally, the Bells’ recent *ex partes confirm* these basic facts. Indeed, the Bells have effectively abandoned any argument that competitors can economically construct their own loop and transport facilities when they only need transmission capacity below the Commission’s previous thresholds. Rather, their argument for broad elimination of unbundling now rests almost entirely on the availability of special access, which we address in Section III, *infra*. Moreover, the Bells’ various maps of competitive loop and transport deployment now effectively *concede* that competitive self-deployment of alternative transmission facilities is quite limited. And the remainder of the Bells’ evidence is entirely consistent with the Commission’s previous findings that competitive deployment of loops and transport is limited to routes on which competing carriers have more than 2 or 12 DS3s of capacity, respectively.

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A. AT&T's Deployment Data Confirm That The Capacity Thresholds Are Actually Over-Predictive Of Non-Impairment.

In the *Triennial Review Order*, numerous parties (including AT&T) submitted cost studies and other evidence demonstrating that competitors are impaired in their ability to construct facilities on any given loop or transport route unless they have a minimum number of DS3s of *committed* traffic. The Commission concluded that the economic breakpoints for the feasibility of self-deployment were 2 DS3s for loops and 12 DS3 for transport – conclusions the incumbents have never directly challenged and that were not criticized by the Court. *See Triennial Review Order* ¶¶ 324, 388-89. The Commission has far more evidence available to it today, however, and those data even more strongly confirm the basic correctness of the Commission's judgments regarding non-impairment. As shown below, AT&T has conducted an analysis of all of its actual loop and transport deployments since 2003, and this experience confirms not only that deployment is infeasible below the Commission's traffic thresholds, but also that the Commission's thresholds were considerably generous to the incumbents. Moreover, AT&T also provides the Commission with a business case analysis demonstrating that a carrier which seeks to deploy a loop that will carry only 2 or fewer DS3s of traffic cannot possibly do so economically unless it – by chance – has a metropolitan fiber access point that is *directly in front of* the building to be served. In addition, the capacity limitations applicable to transport are reasonable – provided the limitation is applied solely to the subset of dedicated transport identified as “entrance facilities.” Indeed, if anything, the evidence before the Commission demonstrates that its previous capacity limitations are reasonable only with respect to loops when the competitor's metro fiber is within 500 to 1000 feet of the building and with respect to transport when the competitor seeks to connect its network to an incumbent LEC wire center that is within 1 mile.

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It is important to underscore that competitive carriers are in a fundamentally different position than incumbents. The incumbents historically were protected monopolists that were guaranteed the ability to serve all demand in their franchised territories. They were permitted – and provided inducements – to construct a ubiquitous network consisting of fiber facilities connecting their wire centers to each other and fiber loop feeder plant reaching deep into many neighborhoods. Today, at least the Bells connect each and every wire center (LSO) with fiber and have extended fiber to virtually every enterprise customer location of any size, and this fiber has substantial excess capacity, because these fiber cables were rationally deployed with numerous spare strands. Fea-Giovannucci Dec. ¶ 29.

Now that the incumbents' fiber infrastructure is already in place – and close to virtually every customer location (whether wholesale or retail) – incremental increases to the incumbents' capacity and reach can be made at extraordinarily low incremental costs compared to those faced by any competitor. For example, suppose an incumbent has two LSOs connected with fiber and an OC-48 multiplexer at each end that currently carries 28 DS3s of demand at the optical level. That incumbent could serve 20 more DS3s of demand on those facilities – more than a 70% increase – *without a single dollar of additional investment*. And it could serve more than 3 times that demand (a total of 96 DS3s, or 68 additional DS3s) by investing only about \$20,000 (\$5,000 for a new line card at each end plus a set of fully redundant cards as back-ups). The incumbent's incremental investment is thus less than \$300 per DS3 – and more likely \$0. In comparison, a new entrant could easily face an investment of over \$1 million for the terminal multiplexers and outside plant required (assuming the LSOs are several miles apart) to connect those same offices and deliver the same capacity. Thus, even at a demand level far above the proposed capacity

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limits, the competitor would face an investment many times that of the incumbent. Fea-Giovannucci Dec. ¶ 28.

Thus, the vast majority of the incumbents' transmission networks could never be economically duplicated by a competitor. A competitor can construct its own facilities only over very short distances where it has enormous traffic, such that its costs begin to approach those of the incumbent – either loops for retail customers, which are close to the competitor's existing network or entrance facilities from an incumbent LSO to the competitor's network. This is exactly what happens in the marketplace. In each of these cases it is somewhat less likely that the incumbent has existing fiber in place, but even if it does, the incremental construction for the competitor (assuming it has an existing metro fiber ring in place) is limited to a very short distance (*e.g.*, a city block or two) so that its incremental cost disadvantage is reduced from one or two orders of magnitude higher than the incumbent's to only about 1 to 2 times that of the incumbent.⁷

1. **Loops.**

The Commission previously found that competitive deployment of loops is uneconomic (and competitive carriers would thus be impaired) at any given customer location unless a competitor has more than 2 DS3s of traffic at that location. *Triennial Review Order* ¶ 324. That

⁷ Moreover, the availability of special access is irrelevant to this analysis. The real inquiry is how the competitor's incremental costs compare to the incumbent's incremental costs. The incumbents' incremental costs are far below their special access rates (and below their UNE rates, for that matter). In any situation in which the incumbent's incremental costs are below the competitor's costs, the incumbent always retains the ability to drop its retail prices and thus render the competitor unable to compete. In this respect, to the extent that the Commission's analysis in the *Triennial Review Order* was based on comparisons of competitors' costs to special access rates, *see Triennial Review Order* ¶ 388 & n.1205, that analysis was extremely generous to the incumbents.

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conclusion remains correct. Virtually all of AT&T's *actual* and *potential* loop deployment occurs above the 2 DS3 threshold.

Indeed, the Commission's 2 DS3 threshold is quite generous to the incumbents, because there are in fact many cases in which a competitor would need considerably more than 2 DS3s of traffic to make self-deployment economical. This is true because the economics of loop deployment are in fact a function of *both* traffic (capacity) *and* distance. Competitors build metropolitan transport networks first, and then they deploy loops to individual buildings solely as extensions from that pre-existing metropolitan transport network, and only where the incremental investment is justified. Thus, regardless of how much traffic a competitor may have at a customer location, it would build loop facilities *only* to locations where it already has enough overall traffic to have built a transport network, and then only to commercial locations that are very close to its existing fiber facility.⁸ The farther a customer location is from the competitor's existing fiber backbone, the greater the cost of deployment, and therefore the more incremental revenue the competitor must realize to justify any new facilities deployment. In the context of loop deployment, outside plant costs are so high that *only a few hundred feet* (*i.e.*, one or two city blocks) can make all the difference: a competitor may have fiber on a street, but if the nearest splice point on its facility is down the street at the next intersection, the additional distance

⁸ This is partly why the Commission was correct to establish a lower traffic threshold for loops than for transport. Loop facilities are typically much shorter than transport facilities. In addition, loop construction is usually based upon new end-to-end revenues for service, whereas transport deployment is justified based on avoidable costs on only a portion of an overall end-to-end service. Thus, loop construction typically involves shorter segments of outside plant, and the costs of construction are offset by higher benefits (revenues/expense savings) per DS3. *See* Fea-Giovannucci Dec. ¶ 24.

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(which requires additional outside plant costs) may render the investment uneconomical. *See* Fea-Giovannucci Dec. ¶¶ 34-36.

This is clearly demonstrated in the Declaration of John D’Apolito and Milford Stanley, which walks through AT&T’s business case for deploying loops to new customers that commit new revenue. Messrs. D’Apolito and Stanley analyzed the thousands of actual business cases AT&T has undertaken since the beginning of 2003, determined the typical investment in electronics and outside plant and the typical revenues and commitment period associated with DS3-based services, and then determined the minimum number of DS3s that would be required to generate a profitable business case under varying conditions – most importantly, the unit cost and length of outside plant required to reach a customer’s location. The results confirm that deploying loops to serve only 2 or fewer DS3s of traffic – and *a fortiori* any DS1 demand – is almost never economical, and more and more traffic would be necessary to justify deployment the farther the customer location is from AT&T’s existing fiber.

The two biggest cost drivers in loop deployment are the investment in incremental outside plant and the electronics that must be placed at each end of the connection. Virtually all loop deployment requires the placement of new outside plant (conduit and fiber) that connects a pre-designed access point on pre-existing AT&T metro fiber to the customer’s location.⁹ In the vast majority of cases, the competitive carrier must extend a fiber lateral to the location in an underground conduit. The conduit is by far the most expensive aspect of outside plant cost. The conduit cost is driven by the cost of opening a trench, placing and stabilizing the conduit, and

⁹ A very small percentage of AT&T’s loops are provided over broadband wireless connections, but the conditions that would allow AT&T to use fixed wireless loops are very rare. *See* D’Apolito-Stanley Dec. ¶ 16, n.6.

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then closing the trench. Outside plant costs are highly distance-sensitive and can vary within a wide range, but for purposes of this analysis AT&T is using the publicly available HAI figure of \$125,000 per mile, which is very close to AT&T's own observed costs. *See* D'Apolito-Stanley Dec. ¶ 16 (giving AT&T proprietary data on outside plant cost).

Loop deployment also requires optical terminal equipment that is placed at both ends of the new fiber connection, which is necessary to "light" the fiber.¹⁰ The cost of such equipment varies based upon the total bandwidth capacity that is being supported (*e.g.*, an OC3) as well as the subunits of capacity that will be activated (*e.g.*, a DS3). For purposes of this analysis AT&T is using the publicly available HAI-derived figures of \$23,600, which again is close to AT&T's own observed actual costs. *See* D'Apolito-Stanley Dec. ¶ 15 (giving proprietary data on AT&T's actual electronics costs).¹¹

Once AT&T has obtained an estimate of the construction cost, it then identifies all new revenues and/or expense savings to which the customer would be willing to commit. On average, an approved business case (*i.e.*, a case in which the economics allow AT&T to make a

¹⁰ Where a terminal has already been deployed at the location, the carrier may only need an additional plug-in card to add capacity to a previously deployed add/drop multiplexer common equipment. These cards represent an investment that generally runs between \$5,000 and \$10,000, depending on the card's capacity. Two cards are needed (one at each end) for such installations. This demonstrates that the costs of increasing capacity at an already-served location may be orders of magnitude less than the costs of creating the initial connectivity. This is one of the key reasons why incumbents have such huge advantages compared to competitive carriers.

¹¹ The AT&T business case also reflects the opportunity cost of using capacity on the pre-existing metro fiber (*i.e.*, allocated capital), operating expenses for supporting the services, and other cash expenses such as income taxes, property taxes, as well as incumbent access at the far end of the circuit. It also incorporates a terminal value of the assets at the conclusion of the contract, which avoids burdening the initial sale with the total investment, because some customers renew their commitment. D'Apolito-Stanley Dec. ¶ 18.

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customer proposal that requires new construction) generally involves a 3-year contract term and generates about [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] per month in combined revenues and cost savings, an amount that is far beyond the revenues implicit in the sale of only one or two DS3s of capacity. D’Apolito-Stanley Dec. ¶ 19. Because the Commission’s rule is based on DS3s (*i.e.*, capacity) rather than revenues, AT&T has estimated the typical unit revenue for committed DS3s, which is [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] per month. An independent and publicly available estimate is based on what a DS3 special access configuration might cost if it were bought under a multi-year commitment. This figure is a reasonable proxy for AT&T’s experience and is \$3,382 per month.¹² This estimate is again conservative for present purposes, because it is higher than the observed recent business cases that explicitly identified DS3 private line revenue commitments. See D’Apolito-Stanley Dec. ¶ 19.

As Messrs. D’Apolito and Stanley explain, given the cost of the infrastructure and the revenue generated by a typical DS3, a carrier could not economically deploy a loop to a location to serve 2 DS3s of committed capacity unless the outside plant mileage is only 0.3 city blocks – or about 88 feet¹³ – based on average costs for constructing outside plant. In other words, a

¹² A reasonable estimate of the cost of a special access DS3 channel termination (the equivalent of a DS3 UNE loop) is \$1,300 per month, and an interoffice channel costs about \$588 per month plus \$57 per mile per month, based on an arithmetic average across all RBOC density zones and rate types. Thus, a 10-mile end-to-end connection costs about \$3,758 per month ($2 * \$1,300 + \$588 + 10 * \57). A CLEC would likely need to price 10% below this level, or \$3,382 per month, to win the business. The AT&T business case evaluation assesses the incremental cost of placing a customer location on-net and providing an end-to-end circuit. As such, the comparison to an access configuration with a channel termination (*i.e.*, loop) on each end and an interoffice circuit connecting the two is reasonable.

¹³ We assume for these purposes that an average city block is 350 feet long.

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carrier could not economically deploy a loop to serve only two DS3s of capacity unless it literally has an access point to its metro fiber *immediately outside the front door* of a building location. See D’Apolito-Stanley Dec. ¶¶ 21-22.¹⁴ The likelihood of this occurring in any individual case (and thus being predictable in advance, which is necessary to implement a regulatory rule) is practically zero, since splice points on competitive networks are typically placed about 2,000 feet apart. Fea-Giovannucci Dec. ¶ 23.

Moreover, even if one considers very broad variations in outside plant costs, the conclusion remains the same, because even under the most extreme favorable assumptions, a carrier could not economically deploy a loop to serve only 2 DS3s of demand unless the building were no more than one city block (350 feet) from the carriers’ existing fiber. The following table illustrates the point:

Unit investment in OSP Capital/Mile	Maximum Off-Net Distance for 0 NPV (2 DS3s)
\$31,250	350 ft
\$62,500	175 ft
\$125,000	88 ft
\$250,000	44 ft
\$375,000	29 ft

¹⁴ For simplicity, the business case does not add costs that reflect the fact that the capital costs must be incurred well before the customer’s circuits are activated and produce a single dollar of revenue. Modeling this “real world” condition would only make it more difficult to prove in the construction, because it would add capital return requirements during the construction and pre-service period.

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These data demonstrate two critical points: First, they explain why the fact that one carrier serves a particular building cannot be dispositive as to whether it would be economic for another carrier to serve the same location at the same level of demand. Second, it demonstrates that there are virtually no circumstances under which a CLEC could afford to construct a new facility to serve only 2 DS3s of demand if the nearest access point on its metro ring is more than about a block away.

In addition, it is important to underscore that this analysis is limited to the purely *economic* question of whether a carrier has enough demand to cover the costs of construction. As discussed below in Section II.C, there is a wide array of circumstances in which a carrier may be prevented from actually constructing facilities even if a carrier can economically justify construction. These circumstances include cases where the carrier cannot obtain (i) the necessary rights of way or permits required for construction, (ii) necessary building access from the landlord, or (iii) customer approval to move its traffic onto newly constructed facilities. *See* Fea-Giovannucci Dec. ¶¶ 40-46; *see also Triennial Review Order* ¶ 209.

This analysis dramatically confirms that a 2 DS3 capacity limit is significantly *over-predictive* of non-impairment for competitors. When a carrier's nearest network access point is more than just a very short distance from a building location, the costs of network extension rise rapidly, and the carrier would need far more than the revenue from 2 DS3s of capacity to support new construction. As the distance between a building location and the nearest access point on an existing CLEC metro fiber increases – particularly when, as is typically the case, the carrier must construct a new conduit – the carrier's ability to justify deployment of even higher capacity facilities diminishes rapidly. *See* D'Apolito-Stanley Dec. ¶¶ 20-22.

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This analysis also underscores why the relevant geographic market for loop deployment must be both location-specific and carrier-specific. While one competitor may find it economically feasible to construct a lateral from its metro fiber to a particular location – because of its unique circumstances with regard to committed traffic and a short distance of the customer location from its fiber network – that does not mean that any other carrier whose nearest pre-designed access points is farther away could deploy loops to that same location at the same capacity level. Indeed, the fact that a competitive carrier can only afford to construct very short “laterals” from pre-designed access points on their metro fiber explains why one carrier may find it feasible to serve a building and another carrier – whose fiber access point may be only one or two blocks more distant – cannot serve the same building with its own loop facility.

As discussed in more detail in Section II.C, *infra*, the Bells’ own data confirm this random and sporadic pattern of loop deployment. Accordingly, it would be incorrect to assume that one carrier’s deployment to any particular location means that any other competitor could deploy loops to that location, or that any competitor could deploy loops to any other location, whether in the same MSA even on the same city block. Moreover, even in the limited instances where a particular competitor has both the necessary committed revenues and a very nearby access point to its metro fiber, it can still be foreclosed from constructing its own facility if it cannot obtain a building permit from the municipality, the landlord refuses to provide reasonable

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and timely building access or the customer declines a request to move its traffic to the competitor's new facilities. Fea-Giovannucci Dec. ¶ 40-46.¹⁵

It is also important to emphasize that the incumbents are *not* “similarly situated” with competitors respect to loop deployment. Even in the relatively uncommon cases where the incumbent does not already serve a particular building with fiber, its ubiquitous fiber network generally has accessible fiber located very close to the customer's building. Accordingly, the incumbent can generally self-provide such facilities at costs far lower than a rival. The competitor's costs to construct a new loop facility are not only fixed and sunk, they are also incremental, in that the competitor cannot provide the service without incurring them. In contrast, in most cases, the incumbent is *already* serving the location with its own fiber, which means that it can match a competitive offer without incurring *any* incremental cost to provide the services the competitor is proposing – it is already doing so and has substantial room between its price and marginal cost to do so. At worst, the incumbent would only need to augment its existing terminal multiplexers by inserting plug-in cards (into a pre-provisioned empty slot) at each end of the new circuit for a total investment on the order of \$10,000 to \$15,000 – an investment far less than the competitor's. See D'Apolito-Stanley Dec. ¶¶ 25-26.

Given this analysis, it also must go without saying that there are no likely circumstances in which it would be economic to deploy a loop facility for DS1-based circuits. Because the fixed costs of construction are so high, a competitive carrier cannot recover its investment and

¹⁵ This is further confirmed by Messrs. Fea and Giovannucci, who describe an AT&T “cluster” build project in Jacksonville, Florida. AT&T analyzed loop deployment opportunities at a number of buildings within a small geographic business district within Jacksonville. Out of 24 buildings examined, fourteen had enough traffic to justify deployment, while the other ten – some of them in the same block on the *same streets* – did not justify the cost of construction. See Fea-Giovannucci Dec. ¶ 62.

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operating costs if the revenue or access saving yield is limited to one or a few DS1s. As a result, the Commission correctly recognized that the expected revenues from the provision of stand-alone DS1-based loops are obviously insufficient to support competitive construction costs. *TRO* ¶ 325 n.957 (record “evidence *does not* support the ability to self-deploy stand-alone DS1 capacity loops nor does it impact our DS1 impairment finding”).¹⁶ The Commission was therefore undeniably correct that competitive construction of DS1 facilities is so unlikely that there was no point in adopting a “self-provisioning trigger” for either DS1 loops or transport. *Triennial Review Order* ¶ 327. And given that the vast majority of even “near-net” locations AT&T serves with special access are served with only DS1 level facilities, *see* Fea-Giovannucci Dec. ¶ 59, this also means that the vast majority locations served with high-capacity loop facilities are characterized by impairment.

Thus, it should not be surprising that AT&T obtains nearly all – more than **[BEGIN CONFIDENTIAL]** **[END CONFIDENTIAL]** – of its total DS1s (purchased as DS1s) from incumbents. AT&T obtains only a very small amount, **[BEGIN CONFIDENTIAL]** **[END CONFIDENTIAL]** of its total DS1s from competitive carriers, and self-supplies the small remainder, generally over facilities it has built to provide much higher capacity services.¹⁷

¹⁶ *See id.* ¶ 391 (“A carrier requiring only DS1 capacity transport between two points typically does not have a large enough presence along a route (generally loop traffic at a central office) to justify incurring the high fixed and sunk costs of self-providing just that DS1 circuit. This is because a requesting carrier in need of DS1 capacity transport faces the same fixed and sunk costs as other carriers deploying transport or using alternatives, but faces substantially higher incremental costs across its customer base than a carrier requesting higher capacity transport”).

¹⁷ For example, if AT&T has placed a building on-net to support a 100 Mbps LAN connection, it may also place other demand of that customer (such as a few voice DS1s) onto the same facility. Fea-Giovannucci Dec. ¶ 64.

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AT&T also obtains [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] of its *total* DS3 loops (purchased as DS3s) from incumbents, self-supplies about [BEGIN CONFIDENTIAL] [END CONFIDENTIAL], and obtains the small remainder [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] from competitive suppliers. And it should be recognized that these facts are fully *consistent* with the 2 DS3 capacity threshold for loops. The fact of the matter is that, for most of the buildings to which AT&T has deployed loops, AT&T serves many more than 2 DS3s. As a result, even though AT&T has a substantial proportion of self-provisioned DS3s loops, it is virtually always uneconomical for AT&T to build loop facilities to a building unless it has more than 2 DS3s of total demand at that location. *See* D’Apolito-Stanley Dec. ¶¶ 20-22. Virtually all of AT&T’s self-supplied DS1 and DS3 loops are used to serve customers in locations where AT&T has *already* built *higher* capacity facilities and where those same customers have a variety of needs (including a need for smaller capacity services). This is fully consistent with the principles the Commission announced in the *Triennial Review Order* and that *USTA II* did not criticize. *See Triennial Review Order* ¶ 298 n.859 (“[i]n limited cases where evidence exists that a competitive LEC is serving customers via their own DS1 loops, the record suggests this is largely because these competitive LECs have already self-provisioned OCn level capacity to that specific location and other deployment barriers have not precluded them from using that capacity to serve other customers at lower loop capacity levels at that same location”).

2. Transport

The Commission’s previous determinations with respect to transport are also correct in the limited circumstances in which it is economically viable for competitive carriers to build transport – *i.e.*, for entrance facilities. The Commission previously found that competitive deployment of transport would be uneconomic (and competitors would thus be impaired) on any

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point-to-point route unless that carrier had more than 12 DS3s of traffic on that route. *Triennial Review Order* ¶¶ 388-89. It remains true that virtually all of AT&T's *actual* and *potential* transport deployment occurs above the Commission's 12-DS3 traffic threshold. But these concentrations generally occur *only* at the last incumbent wire center (LSO) before the hand off is made to the competitor's network over the transport facility known as an "entrance facility."

The Use of ILEC Transport in Competitive Networks. Because of the huge expense required, competitive carriers deploy very short dedicated transport links for one purpose: to carry traffic aggregated at an ILEC wire center to the competitor's own network. Indeed, the distance-sensitive costs of deploying outside plant are so great, and the distances involved with interoffice transport are so long, that competitors almost *never* deploy transport links to connect one ILEC wire center to another – *i.e.*, what one is traditionally called "interoffice transport." ILEC wire centers are often at least several miles apart, and competitive carriers would rarely have enough traffic to justify the cost of constructing the length of outside plant cost required to self-deploy an alternative to such ILEC transport. Rather, competitive transport deployment consists almost exclusively of entrance facilities – very short transmission links connecting the competitive carrier's network to ILEC wire centers where the competitor has aggregated a large amount of traffic. In almost all cases, the only access charges that self-deployment of "transport" allows the competitor to avoid are the incumbents' exorbitant channel termination charges, not those for distance-sensitive interoffice transport.¹⁸

¹⁸ Indeed, because a facility connecting two ILEC wire centers has no re-use value to a competitor, its impairment is severe and the true test of impairment is must be a comparison between the competitor's cost for the incremental capacity compared to the incumbent's cost for its incremental capacity in the same situation. As discussed above and in the accompanying declarations, this differential is so great in favor of the incumbent, that national impairment, regardless of capacity, would be a justifiable conclusion for LSO-to-LSO connections.

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Because an entrance facility is a transport route connecting the incumbent's network and a competitive carrier's network, the competitor is much more likely to have high demand densities at the ILEC LSO where the connection is established. And when the competitor's nearest node is relatively close to the ILEC LSO where the entrance facility connects the two carriers' networks, incremental outside plant construction costs are reduced to levels that may support a business case.

On the other hand, on a route between two ILEC LSOs, a competitor generally has only a small fraction of the demand carried over an entrance facility. Indeed, competitors use transport between ILEC LSOs for the very purpose of aggregating traffic at hub locations where they can attain the highest traffic volumes and may thus be able to support their own entrance facilities. And critically, LSO-LSO routes are typically much longer than the short distances for which entrance facilities may be economic. On average, ILEC LSOs are typically on the order of 5 to 10 miles apart – making outside plant construction costs prohibitive. As a result, there is little if any actual competitive construction on LSO-LSO routes.¹⁹

This explains why it is so important for competitive carriers to obtain access to unbundled transport between ILEC wire centers. Competitive carriers build their own transport to nearby ILEC wire centers that act as a hub for their traffic from customers served out of many ILEC LSOs in an area. Unlike the incumbent, the competitive carrier will only be able to serve a small number of DS3s on each of those subtending LSO-LSO transport links, and it would never

¹⁹ Given these facts, it can be seen that the incumbents are actually seeking to use the limited instances of *entrance facility* construction as a basis for creating a broad prohibition on unbundled access to UNE transport that connects ILEC wire centers. Since competitors cannot afford to construct LSO-LSO transport – and in fact need that functionality to be able to aggregate traffic efficiently – broad elimination of dedicated transport will simply reinforce the ILECs' already enormous natural monopoly cost advantages over their competitors.

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be economic for the competitive carrier to deploy alternative facilities on such routes because it could never even remotely match the incumbent's economies of scale. The only possibility for the competitor to do so is if it can collect sufficient traffic (using cost-based UNEs) to make it economic to construct facilities that connect to its own network. Thus, access to unbundled transport is critical to *encourage* facilities-based entry, as the Commission previously found. Unbundled access allows competitive carriers to lower their cost for the subtending links, which allows them to acquire the traffic they need to justify deployment of alternative facilities. *Triennial Review Order* ¶ 370. And, of course, denial of access to such transport at cost-based rates will severely impair competitors' ability to serve in the enterprise market.

In this regard, it can be seen that competitive carriers use transport connecting ILEC LSOs in a manner analogous to the way that incumbents use loop feeder plant. Competitive carriers do *not* carry traffic between two ILEC LSOs as endpoints; rather, they use transport to aggregate demand from multiple ILEC LSOs at a central point (typically a fiber based collocation in another ILEC LSO) where they can then most efficiently use entrance facilities to place the combined traffic on their own networks.

It is also critical to realize that the fact that the same or different competitive carriers have built *entrance facilities* to two particular wire centers says nothing about the availability of competitive supply *between* those two points. It merely demonstrates that those particular carriers had sufficient end-user demand to justify a connecting facility to its own network at those points. In addition, a competitive carrier's selection of a specific LSO as a hubbing point (a location for a fiber-based collocation) says little about the profile of that individual office. Rather, the selection is driven by engineering concerns that are designed to minimize (1) the total transport distance for all of the offices to be hubbed and (2) the cost of construction of an

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entrance facility from the hub to the competitors' nearest available network access point. Fea-Giovannucci Dec. ¶ 15. Thus, an individual competitor's choice of a particular LSO to house a fiber-based collocation says little about whether another carrier would choose to collocate in the same LSO.

All of the above explains why competitive carriers are generally not operationally ready to deliver traffic between ILEC wire center pairs. Competitors do not typically pick up *and drop off* their own customers' traffic between ILEC wire centers pairs, both because it is demonstrably inefficient to do so and because there is little if any such end user demand.

This also helps to explain why DS_n transport *wholesalers* are rarely available. The costs and operational hurdles of wholesaling at the DS_n level, combined with the limited market for such services, are generally not worth the trouble to set up a wholesaling operation. First, because the necessary connections between LSO pairs do not even exist – even when a competitor has a fiber-based collocation in each office – a potential wholesaler would have to incur significant expense to create them. These costs include the purchase and installation of optical/digital conversion capabilities, as well as the costs of setting up the OSS needed to establish a wholesale business. Fea-Giovannucci Dec. ¶¶ 21-22. In addition, a potential wholesaler must incur the significant administrative costs and practical problems associated with making arrangements with the incumbent to enable cross-connections in the ILEC wire center to wholesale customers. As a result, the incumbents can effectively become the gatekeeper of the competitor's wholesale service, to a degree that would make the service too unpredictable to maintain. Finally, it is often the case that a route defined by an ILEC LSO pair will not provide the entire route that a competitor needs for its own traffic. The Commission has already correctly recognized that “daisy chaining” CLEC networks is costly and inefficient. *Triennial*

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Review Order ¶ 402. Indeed, any outages or other problems that might occur in such an arrangement would be exponentially more difficult to manage, which is why competitive carriers generally do not enter into such arrangements. Fea-Giovannucci Dec. ¶ 22. And all of these costs and burdens must be measured against the generally limited demand for DS_n wholesale service – which is exacerbated by the lock-in provisions of incumbent access tariffs (*see* Part III, *infra*) – the available market is generally not worth these costs. For these reasons, among others, AT&T virtually never wholesales DS_n services between its fiber based collocations in ILEC wire centers in a local area. *See* Fea-Giovannucci Dec. ¶ 22.

A 12 DS3 Cap on Transport UNEs is Actually Over-Predictive of Competitive Non-Impairment. Like the cap on UNE loop availability, the Commission’s 12-DS3 traffic threshold for transport is extremely generous to the incumbents. One important reason is because, as with loops, the economics of transport deployment are a function of both traffic and distance. When a competitor is considering whether to build a transport facility between its network and an ILEC wire center, the distance between those points is just as important as the amount of traffic the competitor has on that route. Twelve DS3s would be the minimum amount of traffic necessary to justify deployment of transport on the very shortest transport routes (*i.e.*, entrance facilities), assuming that all other deployment-related costs are also minimized. As the distance increases, the competitor must have progressively *more than* 12 DS3 traffic to justify building its own facilities. And, there comes a point at which the distances will be so great – generally the distance separating two incumbent wire centers – that a competitor would never realistically have enough traffic to justify self-deployment at all. In that respect, the Commission’s 12 DS3 threshold is actually quite over-predictive of cases in which competitors are “not impaired,”

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because there are so many situations in which 12 DS3s would not be enough traffic to justify self-deployment of transport.²⁰

Because of these realities, AT&T deploys transport links only where it has enormous capacity and the transmission segments are extremely short. Almost all of AT&T's self-deployed transport links carry more than 12 DS3s, and often many more than 12 DS3s. Moreover, AT&T frequently declines to build transport links for which it has more than 12 DS3s, because the costs simply do not outweigh the potential benefits. The opportunities to deploy transport links are few and far between, and AT&T has already built transport facilities (virtually all entrance facilities) to almost every ILEC wire center that could economically support self-deployed facilities construction. The rate at which AT&T has been deploying such facilities has been steadily declining; AT&T is deploying only [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] transport links in 2004, and has planned only [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] for 2005. AT&T also has been reducing the overall number of collocations in its local networks, because of the high costs of maintaining such facilities and the inability to justify extending self-provided facilities to those locations. *See* Fea-Giovannucci Dec. ¶ 70.

Critically, in 70% of the ILEC LSOs serving AT&T customers, AT&T does not have enough traffic to fill even *one* DS3 to reasonable levels. There is obviously no prospect that AT&T could construct its own facilities to serve any of those LSOs. Thus, the only possible

²⁰ Given the current state of local competition, there are very few instances in which a CLEC would have more than 12 DS3s of traffic on an ILEC transport facility that carries traffic solely from one LSO to another LSO (on its path to an entrance facility). Even if a CLEC had a higher level of demand on such a path, however, construction still would not be justifiable because of the enormous cost of deploying outside plant over such a distance.

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alternative that AT&T would have in such cases is wholesale transport offered by an incumbent. However, as the Commission recognized in the *Triennial Review Order* (¶ 387) – and as confirmed by data collected in connection with the state impairment cases – those opportunities are exceedingly rare. Indeed, the New York Public Service Commission Staff’s analysis of wholesale transport identified only 37 routes in the *entire state* of New York where wholesale DS3 transport is available from two or more alternate suppliers, and those routes are entirely composed of LSO pairs between only 10 individual wire centers.²¹

It also goes without saying that transport deployment involves very substantial costs. As with loops, the main cost driver is the enormous fixed costs of constructing the underlying outside plant infrastructure, which is largely a function of the length of the transport link and whatever physical obstacles may exist on that point-to-point route. Fea-Giovannucci Dec. ¶ 72.

Unlike loops, deployment of transport also requires substantial make-ready work at each end of the facility. At the LSO end, the competitor must establish a collocation, which generally costs about [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] in non-recurring charges. Even if it already has a collocation, the competitor must install equipment that provides additional power and fiber connectivity, and it also may require additional space for more terminal multiplexers. In addition, a competitor often has to place equipment in its own POP, which requires adding power feeds, preparing additional space, and running additional riser cables. See Fea-Giovannucci Dec. ¶ 72 (giving proprietary data on AT&T’s actual costs).

²¹ Department of Public Service Staff’s Analysis of Switching and Transport Triggers, March 31, 2004, Attachment 6.

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As with loops, the economics of replacing ILEC-provided transport facilities with self-provided transport facilities is both carrier-specific and route-specific. Whether any particular competitor can deploy transport is a function of where that particular carrier's fiber access points are located in relation to the incumbent's LSOs and how existing services currently route to that competitor's network access point when it uses leased incumbent facilities. The mere fact that one carrier has sufficient traffic to justify replacing incumbent-provided access with self-provided facilities says nothing at all about whether other carriers may have enough traffic to do so. Therefore, the existence of one carrier's transport in a wire center does not allow an inference that other carriers could deploy transport even to that wire center, much less in broader geographic markets such as MSAs. Indeed, even the Commission's previous 12-DS3 limit was based merely upon a finding that, when competitors build transport, they virtually always build 12 or more DS3s of capacity. Even the evidence before the Commission before did not suggest that competitors are never impaired when they need 12 or more DS3s. The evidence demonstrates only that competitors that have built transport had enough demand – given the unique characteristics of their specific networks and the outside plant distances involved. There has never been any evidence that such circumstances always exist when a carrier has more than 12 DS3s of traffic on a given route.

3. Entrance Facilities

In the *Triennial Review Order*, the Commission eliminated unbundled access to “entrance facilities,” which it defined as dedicated transport links between an ILEC switch or wire center and a CLEC switch or wire center. *Triennial Review Order* ¶¶ 365-67. The Commission held that such facilities did not fall within the statutory definition of “network element,” because they were assertedly not facilities “*within* an incumbent LEC's transport network, that is, the transmission facilities between incumbent LEC switches.” *Id.* ¶ 366. The D.C. Circuit agreed

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with the competitive carriers that the Commission’s “reasoning appears to have little or no footing in the statutory definition,” but the Court found the record “too obscure” to vacate the Commission’s determination altogether. It “appear[ed]” to the court that such facilities “*exist* exclusively for the convenience of the CLECs,” and that it therefore “seem[ed] anomalous that CLECs do not themselves provide them, presumably [at TELRIC].” *USTA II*, 359 F.3d at 586. The Court noted that if entrance facilities are network elements, then the Commission would be expected to undertake an impairment analysis. *Id.*

Entrance facilities clearly *are* network elements, and there is no reason to treat such facilities differently from other types of dedicated transport. ILEC-deployed entrance facilities, like all other ILEC dedicated transport facilities, are used to carry traffic from a competitor’s customers’ premises to a competitor’s network (*i.e.*, backhaul), and entrance facilities (like loops and transport facilities between ILEC offices) are provided by using the incumbents’ existing ratepayer-funded infrastructure of transmission facilities. Such entrance facilities, like loops and all other dedicated transport, are undeniably “a facility or equipment used in the provision of a telecommunications service;” thus, they are “network elements” for which the Commission is required to perform an impairment analysis. 47 U.S.C. § 153(29).

Nor is there any sense in which these facilities “*exist* exclusively for the convenience of CLECs.” *Cf. USTA II*, 359 F.3d at 586. Incumbents have built many entrance facilities connecting ILEC wire centers to competitors’ switches, which in many cases also allow ILEC customers to communicate with competitive carriers’ customers. They certainly were not built as acts of altruism for the incumbents’ competitors. As such, these ILEC-deployed entrance facilities are just as much a part of “the ILEC network” as other dedicated transport facilities that connect ILEC switches.

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Finally, as shown above, the impairment analysis for entrance facilities is exactly the same as that for dedicated transport between ILEC LSOs. The only differences are that entrance facilities are typically shorter than the LSO-to-LSO transport configurations and, because the ILEC end of the entrance facility is typically a hub location for multiple LSO-to-LSO paths, the total demand traversing the entrance facility link will be much, much higher. Indeed, it is likely that almost all competitively deployed transport links *are* entrance facilities – it is at least true for AT&T. Accordingly, entrance facilities must be made available on an unbundled basis (and free of use restrictions) where the competitor has insufficient capacity to satisfy the Commission’s 12-DS3 traffic threshold for dedicated transport – and would thus be impaired without access to these UNEs. Although the Court apparently believed it might be “anomalous” that competitors would not build entrance facilities for themselves, the truth is that, when competitors have less than 12 DS3s of traffic at an ILEC wire center, they do not – and as the Commission recognized cannot – deploy their own entrance facilities, because they lack comparable economies of scale to the ILEC. Thus, there is no rational reason to apply a different rule for entrance facilities than for dedicated transport. *See* Fea-Giovannucci Dec. ¶ 76.

B. The Data On Competitive Deployment Collected In State Impairment Cases Validate The Commission’s Previously Established Traffic Thresholds, And Demonstrate That There Is No Need To Apply Any Additional “Triggers” To Further Eliminate Unbundled Access To High-Capacity Loops And Transport.

All of the evidence above clearly shows that the vast majority of all *actual* and *potential* competitive deployment of loops and transport occurs at or above the Commission’s previously established traffic thresholds. Accordingly, those data alone support the re-adoption those traffic thresholds as the complete national rule, with no additional “triggers.” But there is even more compelling evidence that shows such a rule is fully supportable and completely consistent with the principles announced in *USTA II*. The data collected in the state impairment proceedings

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dramatically prove that any such triggers would create enormous administrative burdens for the Commission and carriers generally with no countervailing benefits. The QSI Analysis shows that – even after all of the effort expended by carriers and state regulators to identify instances of alternative self-deployment and wholesaling at the identified capacity levels – there are only *de minimis* exceptions to the Commission’s admittedly low trigger thresholds. *See Triennial Review Order* ¶ 388.

After analyzing available data from 12 states (for loops) and 14 states (for transport),²² QSI reached the following remarkable conclusions:

- There are *collectively* only 130 buildings in 12 states (including California, Texas, Florida and Illinois) that have two or more self-providers of loops with less than 2 DS3s of capacity;
- There are fewer than 50 buildings – in all those 12 states combined – where wholesale DS3 or DS1 loops are available;
- There are only a *total* of 55 transport routes in 14 states (including all the above states plus New York) with three or more self-providers of DS3 transport; and
- There are fewer than 50 routes in all 14 states where there are two or more wholesalers of DS3 or DS1 transport.²³

Since these data compilations include information from many of the largest and most densely populated states, they confirm that continued application of “triggers” would not provide any significant offsetting benefits compared to the huge costs of obtaining and updating such

²² In two of the 14 states it reviewed (New York and Washington) the incumbents did not offer any evidence on competitive loop deployment. QSI Analysis at 1.

²³ *Id.* at 2-3.

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data. In short, the QSI Analysis shows that the 2-DS3 and 12-DS3 thresholds result in virtually *no* cases where competitive carriers are unimpaired when UNEs are available at the defined level. In contrast, strict application of the capacity criteria alone result in a host of circumstances in which carriers are still impaired but are denied access to UNEs, *i.e.*, when they need capacity above the threshold but are still impaired.

Thus, it is already clear that the capacity thresholds – without more – are on balance significantly more favorable to the incumbents than to competitors. As the Court recognized, any regulatory rule in this context will result in some under- and over-inclusiveness on both sides. *USTA II*, 359 F.3d at 575. However, given the tiny number of instances in which there are actually multiple alternatives under the triggers – and the broad array of circumstances in which a strict capacity-based rule denies competitive carriers UNEs in the face of demonstrable impairment – it would be improper to allow the incumbents additional opportunities to seek exceptions to the rule without permitting competitors the same rights.

The State Impairment Evidence Confirms That There Are Only A De Minimis Number Of Exceptions To The Capacity Limits. The data collected in state commission proceedings demonstrate that there are only a *de minimis* number of instances of non-impairment that are not already captured by the Commission's 2-DS3 and 12-DS3 traffic threshold rules. For example, although Verizon sought the de-listing of a far greater number of transport routes in New York than any other incumbent did in any other state, the Staff of the New York Public Service Commission ultimately determined that de-listing would only be appropriate on an extremely small number of transport routes in New York. See NYPSC Staff, *Department of Public Service*

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Staff's Analysis of Switching and Transport Triggers (March 31, 2004).²⁴ The attachments to the Staff analysis show that there are only a handful of Verizon central offices where the transport triggers would have been met in the entire state: only 9 offices where DS1 wholesale transport was available from two or more suppliers, and 10 offices where DS3 wholesale transport was similarly available. Similarly, the NYPSC Staff found there were only 18 Verizon wire centers in the entire state where there is DS3 self-provisioning by three or more competitors (13 in downstate and 5 in upstate). And all of the routes identified by these wire centers are overlapping, *i.e.*, the nine Verizon offices meeting the DS1 wholesale test are subsumed within the ten that meet the DS3 wholesale test, and those offices are in turn encompassed within the 13 downstate offices that meet the DS3 self-provisioning test.

In other words, there are a total of only 18 Verizon offices (and a total of 48 individual Verizon routes) in the *entire state of New York* where one of the two DS3 transport triggers would have been met and 9 offices (and a total of 36 Verizon routes) where the DS1 wholesale trigger would have been met. To place this in perspective, there are 162 Verizon wire centers in LATA 132 – which means that there are more than 13,000 routes in that LATA alone for each type of transport.²⁵ Thus, the 44 DS3 self-provisioning routes that the staff identified in LATA 132 represent only 0.34 percent of the total number of routes – which in turn means that the Commission's traffic thresholds were correct 99.66% of the time, even in New York state. And it also means that the *error rate* that would result from application of the Bells' proposed market MSA-wide definitions would be, at best, in that range as well – nearly 100%.

²⁴ The New York data relied upon in the QSI Analysis is taken directly from the New York Public Service Commission Staff Report, without modification. QSI Analysis at 2.

²⁵ The formula for calculating the number of 2-point routes between n locations is $n(n-1)/2$.

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The results are similar throughout the country. Indeed, outside of New York, the incumbents did not even propose to de-list more than a small percentage of transport and loop routes. For example, in Michigan, SBC proposed eliminating access to 27 DS3 routes in the entire state under the self-provisioning trigger, but the assigned ALJ found that *none* should be eliminated.²⁶ The QSI Analysis also shows that SBC sought to eliminate access to only 9 DS3 transport routes in Ohio, 127 in Illinois, 132 in Texas, and 161 in California – all of which obviously represent miniscule fractions of the overall number of transport routes in those states. QSI compiled data on competitive deployment that was generated through substantial – and often contentious – discovery in 14 states.²⁷ After all of that labor, the data from all of those states *combined* show that a total of *only 55 transport routes* would have satisfied the three self-provisioner requirement of the Commission’s DS3 self-provisioning test (48 of which were in New York). QSI Analysis at 17. And the same is true for loops: in Michigan, SBC recommended that unbundled access to DS3 loops be eliminated at 39 locations under the self-provisioning trigger, but the Michigan ALJ recommended delisting of only *three* buildings in the *entire state*.²⁸ And the QSI Analysis shows that there were only a total of *130* building locations

²⁶ See *In the matter, on the Commission’s Own Motion to Facilitate the Implementation of the Federal Communications Commission’s Triennial Review Determinations in Michigan*, Case No. U-13796, Notice of Proposal for Decision, May 10, 2004, pp. 42-43 (ALJ) (“Michigan ALJ Report”).

²⁷ The states from which data were available included Michigan, Illinois, Ohio, Wisconsin, Indiana, Missouri, Oklahoma, Texas, Florida, Tennessee, Georgia, Washington, New York and California. This clearly represents a broad cross-section of the country and many (if not most) of the largest industrial states.

²⁸ Michigan ALJ Report at 26-29.

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in 12 states²⁹ where two or more competitors self-provisioned 2 or fewer DS3 loops and *fewer than 50* buildings where there was any loop wholesaling. *Id.* at 12, 14.

Numerous Barriers to Entry Preclude Deployment Above The Capacity Limits. In contrast to the *de minimis* number of exceptions to the trigger criteria, the Commission must also recognize that a strict capacity-based rule is substantially *over*-inclusive in identifying the cases when competitors are impaired. There is a wide range of circumstances in which competitive carriers may satisfy the capacity thresholds (*i.e.*, which define only where self-deployment *may be* economically viable), but in which other entry barriers still impair their ability to offer service without access to high capacity loops and transport as UNEs. These factors “decisively” establish impairment, *USTA II*, 359 F.3d at 570, and may not be simply ignored. Indeed, the sheer number of such circumstances demonstrates that application of strict capacity limits on UNEs in fact generates far more cases in which competitors remain impaired *above* the capacity limits than there are cases of non-impairment below those limits.

The initial set of circumstances that may preclude impairment are explained in Part II.A above, which shows that if carriers do not already have fiber facilities close enough to the point they need to connect (whether those points are customer locations or ILEC LSOs), they will not be able to support new construction, even if they have met the 2 or 12 DS3 threshold for loops or transport. But there are also many operational issues that prevent competitors from constructing their own facilities even when they otherwise have a “profitable” business case.

First, the need to obtain rights of way can be a significant barrier to entry. Before a competitive carrier can deploy its facilities, it must negotiate a right-of-way agreement with the

²⁹ There were no data gathered on loops in the states in the Verizon and Qwest regions, because those companies did not seek to challenge the Commission’s national findings.

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local municipality where the competitive carrier seeks to provide service. *Triennial Review Order* ¶¶ 303, 371. Although municipalities were happy to welcome the first-mover incumbent, they often demand exorbitant fees and other onerous conditions from second-mover competitive carriers. *Fea-Giovannucci Dec.* ¶ 40. A typical franchise agreement may take between four and six months to negotiate, and AT&T has franchise negotiations (and accompanying litigation) that remain unresolved after several years. *Id.* Further, even after a franchise agreement is reached, a municipality's ratification process can add as much as 60-90 days before construction can begin. *Id.* AT&T has experienced such delays and additional costs across the country. *Id.* Similarly, AT&T must ordinarily obtain permits from local governments to dig up city streets to construct new transmission facilities, and there are often significant delays in this process too. *Id.* Indeed, many major cities have routine "blackout periods" – up to six months a year – in which such construction is prohibited. These problems deter AT&T and other carriers from deploying facilities even where they might otherwise be economical to deploy. *Id.*

In some situations, a physical obstacle prevents self-deployment on a particular route even where there is high demand on that route. *Id.* ¶ 41. The possibilities of such circumstances are endless. For example, New York City has a number of buildings that are protected for historic preservation, which raises the cost of and may even preclude deployment in some cases. *Id.* Similarly, obstacles such as a river or rail track, can raise the cost of deployment to unacceptable levels in any given case. *Id.* As a result, there is no simple "desktop" analysis that covers all of the many factors a competitive carrier must consider before it can perform a business case to determine whether it is economic to construct new facilities of any kind.

In addition to the issues discussed above, which apply to all types of transmission facilities, a competitive carrier faces the added requirement of negotiating access to each

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building when it seeks to deploy its own loops. *Id.* ¶¶ 42-44. This is all too often an independent barrier to entry, as the Commission has recognized. *Triennial Review Order* ¶ 305 (“In addition to delays associated with gaining access to rights-of-ways and permits from local or municipal authorities, competitive LECs face additional barriers with regard to serving multiunit premises due to difficulties and sometimes outright prohibitions in gaining building access. . . . [I]f the entity or individual controlling access to the premises does not allow a competitor to reach its customer residing therein (or places unreasonable burdens on the competitive LEC as a condition of entry), the competitive LEC may be unable to serve its customer via its own facilities, even where a competitive carrier may be ready, willing, and otherwise able to self-deploy the loop”).

Because marketplace realities require that service to be provided to a customer quickly, it often proves impractical or impossible to negotiate access to the entire building, with the result that the landlord permits the carrier to establish only a “fiber to the floor” arrangement (*i.e.*, only allows the competitive carrier to establish a connection to serve a single customer in a building but not other tenants). *Fea-Giovannucci Dec.* ¶ 44. In AT&T’s case, for example, of the 6,500 buildings it serves with its own loop facilities, all but about [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] of those buildings are served with fiber-to-the-floor arrangements. Indeed, even in the buildings where AT&T has deployed its own loop facilities, fiber-to-the floor arrangements force AT&T to lease loops from the incumbent in a *majority* of cases when it seeks to serve additional customers in those buildings. *Id.*

Another very important obstacle to loop deployment is obtaining the customer’s permission to “roll” its circuits off of facilities leased from the incumbent to the competitive carrier’s facilities. *Id.* ¶ 46. Even when the economics are favorable, the carrier must convince the customer to release the circuit (*i.e.*, permit the service to be interrupted for a scheduled and

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hopefully brief period). *Id.* Unfortunately many customers are unwilling to provide the release (and all customers on a facility must provide the necessary releases) because they are satisfied with the current service and do not want to assume any risk of a service disruption. *Id.* In AT&T's experience, even when presented with reasonable financial incentives, approximately [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] of customers will not agree to such a release. *Id.*

Combinations of these various impairments also create an inherent advantage for the incumbent in the *timing* of its ability to offer facilities-based service to a customer. *Id.* ¶¶ 47-49. Even if AT&T obtains all of the necessary authorizations, the actual construction of the facilities usually consumes at least many months. *Id.* ¶ 47. As with any type of construction project, unforeseen problems, including labor and equipment shortages, can delay completion. Even under ideal conditions, it takes a minimum of twelve months for a facility to become "revenue ready" – *i.e.*, ready to provide service to a customer or customers subtending a particular central office. Such ideal conditions include (1) prior existence of any necessary rights-of-way and the ability to obtain an immediate construction permit; (2) availability of collocation space; (3) all construction proceeding without unforeseen delays; and (4) ready access to the customer's premises within the building. *Id.* As Messrs. Fea and Giovannucci describe, these conditions are virtually never always satisfied. *Id.* Indeed, in many cases the difficulties described above can add months, and even years to the process. *Id.* ¶ 48; *see also Triennial Review Order* ¶ 304 ("[t]he record reflects that constructing local loops generally takes between 6-9 months without unforeseen delay").

These delays create a substantial disparity between incumbents and competitors, and they provide the incumbents with a considerable competitive advantage. For example, because

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incumbents have already developed an extensive interoffice facility network, they generally do not need to seek additional rights-of-way or to construct any new conduit. *Id.* ¶ 49. Moreover, if an incumbent has already deployed fiber to the premises, as is usually the case, it can add substantial capacity by merely changing electronics in the central office. *Id.* This is far less cumbersome than the steps that a competitor must complete to create the same capacity. *Id.* Thus, even if the incumbent must modify its existing plant to serve a particular new customer need, its ability to do so is generally limited only by factors within its own control – for example, upgrading electronics to increase fiber capacity, work-force availability considerations or pulling cable through conduits that already exist. *Id.*

This disparity in timing – which is directly traceable to the incumbents’ position as historic, natural monopolies – often means the difference between whether the customer purchases service from the incumbent or the competitive carrier. *Id.* Customers generally will not wait extended periods of time to obtain service, because they usually seek new services or added capacity to address immediate business needs. In virtually all cases, the incumbent generally stands ready and waiting to provide service to a given customer over *existing* facilities. Thus, although a customer might prefer to use an alternative provider, the need for immediate service often trumps that preference.

Finally, as described in greater detail in Part IV, Bells are increasingly using their market power over special access to insist on tariff provisions that effectively “lock-up” all existing high capacity traffic onto their networks. Fea-Giovannucci Dec. ¶ 50-54; Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶¶ 53-61. These “lock-up” provisions are naked exclusivity arrangements that are increasingly precluding AT&T from building its own loop and transport facilities, even in circumstances in which deployment would otherwise be economically feasible.

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AT&T's Proposal. The data on the record here and from the state impairment cases overwhelmingly support the adoption of rules permitting competitive carriers to access unbundled loops at or below 2 DS3s of capacity and unbundled transport (including entrance facilities) at or below 12 DS3s of capacity – and of course all DS1 loops and transport. There is now a compelling record that, at these very limited capacity levels, there is *no evidence* that local markets around the country vary “decisively” with respect to the factors that define impairment. *USTA II*, 359 F.3d at 570. Given these facts, *USTA II* clearly authorizes the Commission to adopt a national rule finding impairment at these capacity levels – with no exceptions.

The evidence also shows that the number of routes that would be *inappropriately* de-listed under the Commission’s capacity threshold rule (because competitive carriers are still impaired) *far exceeds* the trivial number of routes below those thresholds that might have been de-listed under the Commission’s prior triggers. Moreover, the administrative work and costs required for the Commission and carriers to identify the trivial number of “non-impairment” exceptions to the capacity thresholds have already greatly exceeded any possible benefits, especially given the substantial number of cases of actual *impairment* in situations where competitors are already excluded from UNE access.

The D.C. Circuit expressly recognized that the Commission may take account of such administrability concerns when fashioning an impairment rule. *See USTA II*, 359 F.2d at 575 (requiring the Commission to assess the relative “error costs,” in terms of false positives and false negatives, of various rules); *see also* 359 F.3d at 570 (recognizing that “*some over-inclusiveness*” is inevitable in national impairment findings). And, the facts irrefutably show that the Commission’s capacity thresholds alone are extremely “nuanced,” *USTA II*, 359 F.3d at 563, and that they require unbundling (with only *de minimis* exceptions) only when competitors

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are actually impaired – and also deny access to UNEs in many cases where competitors are *still* impaired.. Accordingly, the Commission is clearly not required to go to additional lengths to identify and de-list every last loop and transport route where there may be “no impairment.”

And in all events, the Commission’s prior self-provisioning trigger should not be re-adopted, because it is inconsistent with the Commission’s own theory of impairment. The Commission correctly recognized that impairment is a function of how much traffic a particular carrier has on a given point-to-point route – *i.e.*, impairment is both route-specific and carrier-specific. *Triennial Review Order* ¶ 298. That means that the mere fact that one, or two, or three carriers may have had enough traffic to build on a route – at some time in the past – does not mean that any *other* carrier with the same amount of traffic would be able to build on that same route in the future. *See* Fea-Giovannucci Dec. ¶ 32. Any test that is solely based on past performance necessarily sweeps in cases where a carrier made a mistake and built facilities where it failed to generate sufficient demand to continue in business. And given the unfortunate history of the competitive carrier industry, those cases were all too frequent. There is no longer any question that the capital markets will no longer allow a competitive carrier to build new facilities “on spec.” D’Apolito-Stanley Dec. ¶¶ 6-8. Indeed, the Commission itself has recognized that only *committed* demand is sufficient to support a prospective business case for new construction. *Triennial Review Order* ¶ 303. Thus, past experience is an especially *unreliable* guide to future performance in this context – especially since the exceptions are limited to cases where competitors have facilities that serve generally uneconomic levels of demand. And since the Commission’s prior self-provisioning trigger did not require any of the self-provisioners to offer capacity at wholesale – and the factual record proves that competitors in fact virtually never offer capacity at wholesale – the trigger denies access to UNEs for all

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subsequent entrants, even though they are impaired. Accordingly, the Commission need not – should not – re-adopt a self-provisioning trigger, or any other similar trigger.

A wholesale trigger has more theoretical validity, but it is entirely unnecessary under these circumstances. The data from the state proceedings confirm that the vast majority of competitors do *not* offer wholesale capacity of any kind. The QSI Analysis documents that exceedingly few loop and transport routes would be de-listed even in the largest, most densely populated states. QSI Analysis at 14-15, 18-20. Since the actual availability of wholesale capacity below the Commission’s traffic thresholds is negligible, the adoption of administratively burdensome triggers would not result in any significant de-listing.

However, if the Commission were to adopt some sort of wholesale trigger, it should ensure that the trigger can be easily administered and will not be subject to significant disputes. The only effective way to do so would be to establish a certification process for competitive wholesalers. The requirement of a carrier-certification based process is essential. As the QSI Analysis shows, there was a large discrepancy between the number of routes the ILECs challenged under the wholesale test and the number of cases in which competitors actually identified themselves as wholesalers that met the operational readiness and related criteria of the *Triennial Review Order*.³⁰ The only way to make such a process administrable – and avoid the substantial costs of such disputes – would be to base it on carrier self-certification. Competitive carriers that offer wholesale services have every incentive to comply with a self-certification process, because they would much rather compete with the incumbents’ exorbitant special access

³⁰ A concrete example of this problem is Verizon’s argument regarding wholesaling discussed in Part II.C *infra*.

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rates than with UNEs provided at TELRIC, and if the Commission were to adopt its prior standard, only two such firms are required on any route to cause de-listing.³¹

But before it adopts *any* additional triggers, the Commission must appropriately recognize the substantial disparity between the trivial number of cases of non-impairment that may be identified through the application of any such trigger and the much *larger* number of instances – many of which the Commission itself has already identified – in which competitors remain impaired *above* the capacity thresholds. It would be arbitrary and capricious if the Commission were to adopt “triggers” only to permit additional delisting without also creating mechanisms that permit carriers to obtain unbundled access to UNEs above the capacity thresholds when they in fact face continued impairment. Any other action would even more severely tip in the ILECs’ favor the existing balance between cases of “false negatives” and “false positives.” *USTA II*, 359 F.3d at 575.

C. The Bells’ Data Also Strongly Confirm That Competitive Deployment Is Feasible Only Above The FCC’s Previous Traffic Thresholds.

The Bells’ have submitted a raft of “evidence” in recent *ex partes* that purports to show widespread market entry by competitors using either their own facilities or ILEC special access services. What is striking about these submissions, however, is that the Bells no longer explicitly claim that competitors could readily deploy their own DS1 and DS3 loop and transport facilities. Indeed, the Bells have submitted maps that purport to show locations and routes on which competitive carriers have “deployed facilities.” Critically, even though those maps and other

³¹ Alternatively, or at least on an interim basis until the Commission collects the necessary data, the Commission could require carriers seeking new UNEs to certify that they have been unable to identify two wholesalers on the route. Given the clear paucity of wholesale options as demonstrated by the QSI Analysis, it would certainly be permissible to make a national finding of impairment based on the capacity thresholds until the data on existing routes are finally gathered.

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evidence are riddled with flaws and greatly overstate the extent of competitive facilities-based entry, the Bells' evidence – even taken at face value – strongly confirms the Commission's previous conclusions that competitive deployment is actually quite limited. The remainder of the Bells' evidence is also entirely consistent with the Commission's previous findings that competitive carriers' deployment of loops and transport is limited to routes on which they have more than 2 or 12 DS3s of capacity, respectively.

1. Verizon's Attempt to Limit the Impairment Analysis To The 20 MSAs In Its Region With The Most Traffic Is Misleading.

As an initial matter, Verizon's attempt to equate the special access market as a whole to the small subset of wire centers in its largest MSAs that have the greatest amount of competitive deployment is fundamentally incorrect and paints a very skewed picture of the special access market. Verizon asserts that more than 80 percent of the demand for high capacity special access services in its region is concentrated in only 8% (or 532) of its wire centers, and that more than three-quarters of those wire centers are in the 20 MSAs in Verizon's serving area with the largest amount of high capacity demand. 7/02/04 Verizon Letter at 6. Verizon contends that the Commission can treat this small subset of wire centers as representative of the entire market for purposes of the impairment inquiry. That is incorrect.

First, Verizon has overstated the extent of demand in these "top 20" MSAs by apparently providing its results on a voice grade equivalent (VGE) basis. In other words, Verizon has weighted the purchase of OCn-level services much higher than DS3 and DS1 services. That overweighting is very substantial, because a single DS3 is equivalent to the purchase of 24 DS1s, and a single OC3 is the equivalent of 72 DS1s. Thus, the only thing that Verizon's methodology accomplishes is to identify the small subset of wire centers that have the greatest concentration of OCn-level special access services.

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But that is not the issue; rather, the issue before the Commission is the extent to which competitive carriers are impaired without access to DS3 and DS1 UNEs. And to assess *that* question the Commission cannot limit its inquiry to the 400 or so wire centers in Verizon's region that have the most VGEs. Indeed, Verizon's own data show that there is still a very substantial demand for high capacity facilities outside those limited geographic areas, most of which is undoubtedly DS1 and DS3 services. This conclusion is not surprising, of course, because with the exception of a limited number of commercial locations (for loops) and situations in which an entrance facility is being replaced, it is unlikely that self-construction of facilities is practical given the incumbents' significant cost advantages.

AT&T has independently verified that it purchases a substantial amount of DS1 and DS3 services from Verizon outside those "top 20" MSAs. For example, during June 2004, AT&T purchased a total of over [BEGIN CONFIDENTIAL]

[END CONFIDENTIAL] in DS1 and DS3 level capacity from Verizon. More than one-third of that total (36%) was spent on DS1 and DS3 facilities that were purchased in areas outside of the "top 20" MSAs in Verizon's analysis. Stith Dec. ¶ 23. And even this figure is too low, because it does not include the additional DS1 and DS3 services that AT&T purchases in lower-demand wire centers within those "top 20" MSAs that Verizon has also excluded from its analysis. *Id.*

Verizon's methodology is particularly egregious as it relates to DS1 loops. Of the total that AT&T spent during July 2004 on DS1 and DS3 capacity loop and transport facilities outside Verizon's "top 20" MSAs, over 70% were for DS1 facilities, and more than 60%, or over [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] were spent on DS1 loops alone. *Id.* ¶ 24.

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2. The Bells’ Evidence of Competitive Loop Deployment Is Consistent With the Commission’s Findings in the *Triennial Review Order*.

The Bells have submitted a variety of charts, maps, and other data in an attempt to show that competitors provide service to their retail customers today using either their own loop facilities or ILEC special access. *See generally* 7/2/04 Verizon Letter; 8/18/04 SBC Letter. Ironically, however, the Bells’ evidence strongly *confirms* that competitive deployment of loop facilities to serve specific customer locations – especially at or below the 2 DS3 capacity level – is extremely limited. Although the Bells’ data are seriously flawed and substantially overstate competitive loop deployment, even when they are taken at face value, the Bells’ data simply underscore that competitors are only able to bring customer locations “on net” in relatively rare circumstances. For example, the Bells’ own data demonstrate that even where competitors have managed to deploy loop facilities to one location, they have *not* been able to use their own facilities to serve other customers – even within the same narrow downtown business districts (much less an MSA). This evidence thus confirms two conclusions: first, that the relevant market for loops is building-specific, rather than absurdly large markets such as MSAs; and second, that the economic viability of loop construction, *i.e.*, non-impairment, cannot be assumed without at least reviewing the capacity that will be provided over that facility and the length of the outside plant that a competitor must construct.

The Bells’ Maps Confirm that the Proper Impairment Inquiry is Building-by-Building.

One of the centerpieces of the Bells’ evidence is a host of street maps of large cities that claim to show customer locations served by competitive carriers, either with their own fiber or with ILEC special access. These maps actually confirm, however, that *self-deployment* of loops is in fact

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quite rare.³² Moreover, the Bells' maps offer no insight at all as to the capacity of service provided over the identified competitive facilities. And in all events, the Bells' data are flawed and overstate the instances of actual competitive deployment.

First, even if one accepts all of the Bell data as accurate, they confirm that competitive loop deployment – at any capacity level – is extremely limited. For example, SBC has provided detailed maps of the central business districts of several major cities within its operating territory. These maps alone confirm that there are a relatively small number of buildings that are served by competitive facilities of *any capacity* (including OCn loops, for which the Commission has found competitors are not impaired). Particularly striking is SBC's map of the financial district of San Francisco, which is a very small and densely concentrated subset of the San Francisco MSA. SBC's own data show *only 68 buildings* in that area are served by CLEC loop fiber – less than 10% of the buildings that are served using special access in the same confined geographic area. Similarly, SBC's data show that there are more than 436 instances in which a competitor is using SBC's special access services to serve customer locations on the *same streets* where competitive fiber is in place. Selwyn Dec. ¶¶ 47-49. The same pattern recurs in the Bells' maps of other major cities. *Id.* ¶ 47. There is only one reasonable conclusion that can be deduced from such facts, assuming that competitors are acting efficiently: all decisions regarding competitors' ability to compete successfully are tied to the relevant facts applicable to each individual building. And the business case analysis described above demonstrates that those relevant facts are closely tied to the length of the facilities an individual carrier must

³² The many reasons why the availability of special access does not eliminate impairment are discussed in detail in Section III, *infra*.

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deploy to reach a location and the amount of revenue it can expect to earn to offset the costs of that deployment, both of which are carrier-specific.

Thus, these maps dramatically confirm that competitive deployment is very limited, even in the most dense urban business districts, and also that the relevant market for purposes of the impairment inquiry must be building by building. The Bells' evidence is thus fully consistent with AT&T's evidence that the economics of loop deployment require the building to be very close to the competitive carrier's network, and that competitors often find it impossible or infeasible to deploy loops to buildings that may be only a block away from other buildings to which they have deployed loops.

Further, the Bells' maps do not identify the capacity served over the competitive facilities deployed to any building. If the Commission's conclusion in the *Triennial Review Order* that competitors cannot typically afford to construct a facility to serve fewer than 3 DS3s to a location is correct (and the evidence clearly shows that it is), one would reasonably expect that the vast majority of such construction would be at the OCn level – a level at which competitors are forbidden to buy UNEs. Therefore, the Bells' data – again, even if it were accepted at face value – are simply irrelevant to the question of whether a carrier needing only 2 or fewer DS3s of capacity at a building can afford to build its own loop. Indeed, it would be irrational to rely on the uncategorized Bell data to support a conclusion that competitors have often (if ever) deployed their own loops to serve such limited demand. Selwyn Dec. ¶¶ 34-35.

Finally, the Bells' evidence is also consistent with the Commission's prior recognition that even when the economics may be favorable, individual buildings are often unavailable because of rights of way and permit restrictions, building access problems and customers'

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refusals to permit their circuits to be rolled. *Triennial Review Order* ¶ 205.³³ In short, the Bells' maps confirm that the actual pattern of competitive loop deployment is randomly distributed and scattershot even in the densest areas of enterprise business demand. This utterly defeats any notion that competitors could easily use the fiber that they have deployed in an area to serve *any* customer in that same neighborhood – or even on the same street or city block. Selwyn Dec. ¶¶ 45-46.

Therefore, the Bell maps alone repudiate any contention that the Commission should – or may – de-list loop UNEs on an MSA-wide basis. The mere fact that some competitors have deployed loops (of any capacity) to certain buildings in an MSA cannot possibly mean that competitors could deploy loops at the specific capacity limits defined in the *Triennial Review Order* throughout that entire MSA. To the contrary, the mere fact that a competitor has deployed a loop facility to one building does not even indicate that it could deploy a loop to the building next door. Any assumption that one could extrapolate from the randomly distributed loop deployment that exists and to an entire MSA is absurd; it would obviously result in a massive amount of erroneous de-listing of loop routes in cases where competitors are in fact impaired.

And in all events, the Bells' data overstate competitive loop deployment. The Bells' claims rest largely on data provided by a firm called GeoResults, which has not explained how it derived its data, nor do the Commission or any other party have any way to independently verify GeoResults's conclusions. Critically, there is every reason to believe that GeoResults's data are substantially overstated. Verizon and SBC indicate that GeoResults's data are derived from data in Telcordia's Central On-Line Entry System ("CLONES") database of Common Language

³³ AT&T also demonstrates herein other potential barriers to self-deployment, including barriers created by the incumbents' lock-up tariff provisions.

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Identifier (“CLLI”) codes.³⁴ As explained in the Declaration of Jeffrey D. Beemon, however, Telcordia rarely eliminates obsolete data from the CLONES database (largely because there is no need to do so). Mr. Beemon has determined that approximately forty percent of the total number of AT&T’s CLLI codes and approximately thirty percent of the total number of different AT&T customer locations in the CLONES database are not in active use. Beemon Dec. ¶¶ 6,8. This alone casts considerable doubt on any of GeoResults’s conclusions.

In short, the Bells’ contention that MSAs are an appropriate geographic market is based entirely on the availability of ILEC special access. But as discussed in detail in Section III, *infra*, competitive carriers remain impaired notwithstanding the availability of special access. However, there can be no claim – and the Bells’ own data effectively abandon any such claim – that the MSA or any other larger geographical area can be used to define the relevant geographic market for the self-deployment of competitive loop facilities. *See also Triennial Review Order* ¶ 341 (rejecting MSA as appropriate geographic market in the unbundling analysis).

The Bells’ Competitive Building Count Data Are Overstated. Verizon’s assertion that competitive carriers serve some 48,350 buildings nationwide using their own fiber is not only irrelevant, it is also grossly overstated. It is irrelevant because, as the Commission concluded in the *Triennial Review Order*, aggregated data reported on a national level says nothing about the circumstances under which loop deployment would or would not be economical. The Commission previously found that the appropriate inquiry is whether a carrier has enough traffic on a given route to justify the investment in the necessary electronics and outside plant, and that self-deployment is not feasible unless a carrier has at least 2 DS3s of traffic. Even if the Bells’

³⁴ *See Ex Parte* Letter from Christopher Heiman, SBC, to Marlene Dortch, at 4 (filed CC Docket No. 01-338, Aug. 18, 2004); Verizon makes similar claims. *See* 7/2/04 Verizon Letter, Att. 1.

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building count data were completely accurate, they would be entirely consistent with the Commission's previous conclusions. There are some 3 million commercial buildings in the United States, and therefore even if Verizon is correct, competitors are serving a miniscule fraction (about 1.5%) of the total commercial buildings in the nation (*i.e.*, buildings that would support an unusually high volume of traffic). *See* Selwyn Dec. ¶ 44.

More pertinently, however, Verizon's building count data are a case study in the total unreliability of Verizon's fact-gathering methods. Verizon derives its conclusions by cobbling together building counts for various carriers from a variety of secondary sources, many of which are demonstrably incorrect. Perhaps the most embarrassing example is Verizon's estimate of the on-net fiber of Pac-West Telecomm, Inc. (Pac-West). Attachment 8 to the 7/02/04 Verizon Letter identifies fourteen MSAs in which it claims Pac-West constructed its own fiber optic networks. However, in a recent *ex parte* letter, Pac-West states that "[t]he information being proffered by Verizon as it pertains to Pac-West Telecomm is wrong. In fact, Pac-West owns *no* fiber. Pac-West serves all customers via facilities obtained from other carriers, with much of that being obtained from the ILECs."³⁵ *See* Selwyn Dec. ¶ 40 & Att. 2.

Similar errors abound in Verizon's assertions regarding other competitive carriers. For example, Verizon relies on a 2001 10-K report to claim that McLeod has 1,500 buildings on-net, but McLeodUSA reported in the second quarter of 2004 that it provides service wholly over UNE-L, UNE-P/M and resale facilities. *See* Selwyn Dec. ¶ 39. Verizon claims that KMC has 15,600 "on-net" connections, but the cited press release actually says that KMC has "15,600 buildings connected to KMC's networks," and its website says the company has "1,700 on-net

³⁵ *Ex Parte* Letter from Richard Rindler, Pac-West Telecomm, to Marlene Dortch, at 2 (filed in CC Docket No. 01-338, Sept. 7, 2004) (emphasis supplied).

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buildings.” *Id.* (quoting KMC website). Verizon claims that TelCove has 3,500 buildings on-net, but a Telcove company brochure advertises “direct connectivity to over 2,500 on-net buildings.” *Id.* And there are more examples. *See id.*

In short, these charts – like all of the Bells’ charts based on third-party sources – are wholly exaggerated and untrustworthy. Even if one corrects Verizon’s chart of on-net buildings (7/02/04 Verizon Letter, Att. 9) for the building counts of just four carriers (KMC, McLeod, TelCove and IDT), *41% of the total number of buildings drop out.* Selwyn Dec. ¶ 41. The Commission thus should give this “evidence” no weight. *See also Pac-West Ex Parte* at 2 (Selwyn, Att. 2) (“[i]n view of the clearly erroneous information submitted by Verizon with respect to Pac-West Telecomm, the information being submitted with respect to other CLECs’ deployment of fiber networks must be independently verified before it may be accepted as fact and relied upon by the Commission”).

Verizon’s Expenditure-Per-Building Figures Are Irrelevant To An Impairment Inquiry And Are In All Events Consistent With The Existence Of Impairment. Verizon has also estimated the “total telecommunications expenditures” in each individual building addressed in the 20 MSAs it has chosen to analyze, and it has constructed a chart purporting to show the extent to which competitors have deployed loops to buildings with high overall telecommunications expenditures. *See* 7/02/04 Verizon Letter at 14-15 & Att. 10.³⁶ Verizon asserts that competitors have deployed loops to 65% of the buildings with an annual expenditure of \$6 million or more; to 57% of the buildings with \$4-6 million in total expenditures; to 50% of the buildings with \$2-

³⁶ These expenditures are presumably annual expenditures, although Verizon does not say.

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4 million in total expenditures; but only to 30% of the buildings with expenditures between \$500,000 and \$2 million. *See id.* at Attachment 10.

These figures are simply irrelevant to a determination of impairment. Total demand in a building does not indicate anything with respect to impairment, because impairment is a function of how the competitor's incremental costs compare with the incumbent's in the context of specific demand for an individual customer. The Commission has correctly recognized that competitors build loops only to serve committed traffic, *i.e.* traffic under a contract between an individual customer and the carrier. *Triennial Review Order* ¶ 303. If a competitor could not recover the cost of deployment from committed revenues from its customer in a building, that competitor would not deploy a loop to serve that customer merely in the hope that it could obtain other customers in the same building in the future. *See D'Apolito-Stanley Dec.* ¶ 11. Thus, "total building revenue" cannot be a direct measure of anything related to the impairment inquiry, given that (i) there are typically many customers in a building, (ii) individual customers often do not give a competitor their entire demand and (iii) these figure do not account for the fact that, as the Commission recognizes *Triennial Review Order* ¶ 302, enterprise demand is typically tied up in multi-year agreements, so the amount of revenue opportunity available at an individual building is inherently unknowable. And in all events, total demand data is not publicly available, and therefore there would be no practical means for the Commission to fashion an impairment test based on such data, even if it were relevant.

Fixed Wireless and Cable. Finally, Verizon asserts that its data on competitive fiber understate the true degree of loop bypass, because fixed wireless and cable companies are also providing competition. 7/02/04 Verizon Letter at 15-16. In fact, the use of fixed wireless and cable are so minimal that they add little to the impairment analysis.

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For example, fixed wireless has limited utility as an entry strategy, because the technology requires line-of-sight transmission that is difficult to achieve, especially in dense urban areas. Such connections can be offered only where (1) the carrier has a wireless broadband license; (2) the building owner permits a competitive carrier to locate an antenna on the building roof; (3) there is a line-of-sight path between the antenna and an a similar unit at the competitor's location; and (4) the span distance is short enough to meet the bandwidth and reliability specifications of the customer.³⁷ It is rare that all of these prerequisites are met. Thus, it should not be surprising that competitive carriers use fixed wireless only sporadically. Similarly, only a small percentage of AT&T's loops nationally are provided over broadband wireless connections. D'Apolito-Stanley Dec. ¶ 16 n.6. Thus, the market presence of fixed wireless is so minimal that it is not material to the impairment analysis.

Verizon also greatly overstates the significance of cable competition. Cable networks are designed to reach residential end-users, not business locations. With few exceptions, cable infrastructures generally do not "pass" business locations and thus cannot readily serve the vast majority of office buildings and other business sites. The Commission has previously found that "[r]esidential and small business subscribers, not surprisingly, account for over 96 percent of the reported high-speed lines delivered over cable systems."³⁸ In addition, cable modem offerings generally do not provide the same service reliability and security as ILEC special access offerings. Cable networks do not have the same degree of back-up electrical power as do typical wireline networks, and the "shared platform" nature of cable modem service raises data security

³⁷ See Selwyn Dec. ¶¶ 109-112 (noting that fixed wireless presents issues of service quality and security).

³⁸ *Inquiry Concerning the Deployment of Advanced Telecommunications Capability*, CC Docket 98-146, Third Report, FCC No. 02-33, 17 FCC Rcd 2844, ¶ 45 (2002).

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and transmission performance issues that are particularly important to business customers, who routinely transmit highly sensitive or mission-critical financial and commercial data. *See* Selwyn Dec. ¶¶ 113-15.

Cable providers reported supplying fewer than 16,000 coaxial cable connections to medium and large businesses nationwide at the time the Commission reached its conclusions in the *Triennial Review Order*, and report less than 30,000 such connections today.³⁹ Given that there are roughly three million commercial buildings in the United States, cable connections represent less than one percent of potentially addressable business locations. Cable, like fixed wireless, is so insignificant as an alternative to the incumbents' high capacity services that it should play no role in the impairment analysis.

3. The Bells' Evidence of Competitive Transport Deployment Is Unreliable and Misleading.

The Bells have also submitted an array of "evidence" purporting to show the extent of competitively deployed transport. This "evidence" falls into two categories. First, the Bells have again submitted cobbled-together estimates of competitors' fiber route miles, and they have augmented that with maps of competitors' fiber routes. Even if these data were accurate – which

³⁹ Selwyn Dec. ¶ 115 (citing *Triennial Review Order* ¶ 41 and Industry Analysis and Technology Division, Wireline Competition Bureau, High Speed Services for Internet Access: Status as of June 30, 2002, rel. December 2002). As Dr. Selwyn notes, the most recent IATD report reveals that for the period ended December 31, 2003, five million high speed coaxial cable connections serving new residence and small business cable customers were added, but that only approximately 3,400 new coaxial cable connections were added that served large business subscribers, with the total number of connections to high speed cable connections to large business users still less than 30,000 in total. *See id.* (citing Industry Analysis and Technology Division, Wireline Competition Bureau, High Speed Services for Internet Access: Status as of December 31, 2003 (2004) and Industry Analysis and Technology Division, Wireline Competition Bureau, High Speed Services for Internet Access: Status as of December 31, 2002 (2003)).

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they are not – they are meaningless, because, as with their loop “facts,” they say nothing about the circumstances under which transport deployment is feasible. Second, the Bells have submitted “spider-web” maps in which they have simply drawn lines between competitive carriers’ collocations as if they actually had established dedicated connections between all of these ILEC wire centers. These maps are little short of preposterous; as shown above, competitors typically do *not* establish dedicated transport connections between ILEC offices, nor do they offer such connections at wholesale.

The Bells’ Data On Transport Are Both Meaningless and Overstated. Once again, the Bells have prepared charts listing various competitors and the “fiber route miles” of transport that they have deployed. The Bells submitted the same sort of data last time, however, and the Commission properly saw the irrelevance of such aggregated data. The relevant question is not whether a competitor can economically deploy transport in *some* circumstances (they obviously can) but whether it can deploy *fewer than 12 DS3s of capacity* on an *individual* route. The fact that some competitors have been able to deploy transport on some routes at some capacities says nothing about whether they or any other competitor could deploy transport capacity at or below 12 DS3s on those or any other routes.⁴⁰

But the Bells’ data are overstated and unreliable in all events. For example, Verizon reports that Cablevision Lightpath has 7,000 route miles of fiber – when in fact two separate sources – including Cablevision’s own website – report that the company owns only 2,700 fiber route miles. Selwyn Dec. ¶ 39. Similarly, Verizon claims that IDT Solutions has 10,000 “route

⁴⁰ The Bells have also submitted maps purporting to show the actual routes of competitors’ transport networks. These maps are essentially pictorial restatements of the Bells’ fiber route mile charts, and they are no more relevant.

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miles” based on NPRG’s 2002 CLEC Report, whereas in the 2003 CLEC Report, NPRG reduced that figure to 5,000, and then reported it as “n/a” in its 2004 CLEC Report. *Id.* It is inexcusable for Verizon to rely on the 2002 figure in light of the subsequent report. And IDT in fact has *no* fiber: it acquired the fixed wireless assets of Winstar, and IDT’s most recent 10-Q report indicates that it does not own any fiber. *Id.*

The Bells’ “Spider-Web” Maps Are Misleading And Irrelevant. Verizon has submitted additional maps in which it (1) plots the fiber-based collocations it has identified in a given city and then (2) draws lines connecting each pair of collocations, which are meant to represent routes connecting ILEC LSOs that competitive carriers themselves could “potentially” establish without using ILEC transport UNEs. In other words, Verizon is simply assuming that if a competing carrier has a fiber-based collocation arrangement in both central office ‘A’ and central office ‘B’, it must follow that the carrier has (or could establish) dedicated transport facilities connecting A and B, and that it could and would provide such connections at wholesale to other CLECs. *See* 7/02/04 Verizon Letter at 11-12.

As explained in detail in Part II.B above, these contentions border on the absurd. Verizon does confess, as it must (*id.* at 11), that its maps are not “mean[t] to suggest that there is fiber directly between each of these wire centers.” That is putting it mildly. Indeed, the discussion above shows that it would be irrational to assume that any competitor has established its own connection between many pairs of ILEC wire centers, or would ever do so.

First, because competitors’ networks are “flatter” than incumbents’ and do not rely on competitively provided “tandeming,” competitive carriers deploy dedicated transport principally for the purpose of connecting an ILEC LSO to their own switch or POP, *i.e.*, to provide entrance facilities. That is, they use LSO-to-LSO transport as an extension of customer loops to extend

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their subscribers' traffic to centrally placed collocations, and from there to their service nodes. Thus, competitors' networks operate as a hub and spoke network – a central-point-to-any-point network, *not* an any-point-to-any-point network like the incumbents' networks. *See* Fea-Giovannucci Dec. ¶ 16. And as the Commission found (and we re-prove above), competitors cannot economically deploy such transport facilities unless they (1) have aggregated enough traffic at an ILEC LSO (*i.e.*, at least 12 DS3s) to justify the high fixed costs of the necessary electronics and outside plant and (2) only have to extend their networks a short distance.

In other words, competitive carriers typically do not construct transport facilities to connect two ILEC wire centers. Accordingly, even if a competitor has deployed transport in a physical “ring” that has some individual strands terminating in two different ILECs LSOs as well as its own service node, the purpose of the *entire facility* is to bring customer traffic back to the node. The competitor would almost never establish dedicated connections *between* those two ILEC LSOs; such a connection is typically unnecessary because a competitor rarely if ever has the need for dedicated connectivity that begins *and ends* between the identified ILEC offices. And since competitors do not need to (and generally cannot afford to) establish a wholesale service between such locations, the likelihood of wholesaling on such (non-existent) competitive routes is exceedingly low. *See* Part II.B, *supra*. Indeed, the data from the state impairment cases show that wholesaling of DS_n level transport is virtually non-existent. *See* Fea-Giovannucci Dec. ¶¶ 18-23; Selwyn Dec. ¶¶ 50-59.

III. THE EXISTENCE OF SPECIAL ACCESS SERVICE PROVIDES NO BASIS FOR DENYING ACCESS TO LOOPS AND TRANSPORT AS UNES FOR LANDLINE LOCAL AND LONG DISTANCE SERVICES.

Given the very limited extent to which there has been self-supply of high-capacity loop and transport facilities – and the overwhelming economic evidence that deployment is uneconomic below 2 DS3s for loops and below 12 DS3s for transport – the Bells' primary claim

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is that the availability of loops and transport at above-cost rates under their special access tariffs eliminates impairment. 7/2/04 Verizon Letter at 19. They note that interexchange carriers and competitive carriers are now using tariffed special access services to provide long distance and certain local services to enterprise customers. On this basis, they assert that competitive carriers will not be competitively “impaired” if they are limited to using only special access hereafter and are categorically denied access to high capacity loops and transport as UNEs even when impairment otherwise exists.

This claim does not withstand even cursory scrutiny. As detailed below, Bells are today providing special access services at rates, and levels of performance, that effect price squeezes and that have foreclosed competitive carriers from providing a broad array of local landline services in competition with the Bells’ retail services where loop and transport UNEs are unavailable. The Bells will have the ability and incentive to effect such price squeezes for all local and long distance services used by enterprise and other business customers in the future if competitive carriers are relegated to special access service and cannot access high capacity loops and transport UNEs. Because federal and state special access regulations afford no protections against price squeezes and other such ILEC abuses, it is axiomatic that the existence of tariffed special access affords no basis to deny access to UNEs where impairment otherwise exists. Indeed, the very reason why Congress required that UNEs be provided at cost-based rates is to prevent the Bells from undertaking predatory price squeezes that would threaten the vibrantly competitive long distance market that existed in 1996.

Although the Bells rest their contrary claims on *USTA II*, it provides them with no support. The Court did not even mention the existence of special access in its explanation of why it was vacating national impairment findings for transport UNEs (and did not address at all

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the Commission’s national impairment findings with regard to high-capacity loops). *USTA II*, 359 F.3d at 573-75. Rather, in vacating the rule that granted wireless carriers access to transport UNEs, the Court relied on the grounds (1) that it was undisputed that wireless carriers had been providing service in competition with incumbents for 20 years by obtaining the incidental transport facilities used in wireless networks under special access tariffs and (2) that the Commission justified extending rights to wireless carriers solely on the basis of its earlier rule that treated the existence of tariffed special access as irrelevant to unbundling determinations. *Id.* at 575-77. The Court held that this blanket rule had not been adequately justified and indicated it could not rationally be applied to wireless carriers because there was no evidence that ILECs had any substantial ability and incentive to “hike” special access rates for wireless services or otherwise to effect price squeezes. *Id.* The Court thus vacated the blanket rule.

At the same time, the Court expressly identified the factors that would allow the Commission either to re-adopt this same rule on remand (particularly for landline services) or to find that the existence of special access does not eliminate the impairment that otherwise exists for high capacity loops and transport for landline services. It noted that because of the “ILECs’ incentive” to set the special access prices “as high as possible” relative to the ILECs’ retail rates and “the vagaries of determining when that price gets so high that the ‘impairment threshold’ has been crossed, “real administrab[ility] issues” can arise if the Commission must assess the competitive significance of special access, and that “these complications” could “support a blanket rule treating the availability of ILEC tariffed services as irrelevant to impairment.” *Id.* at 576. The Court also agreed that “tariffed services ‘present different opportunities and risks for the requesting carrier than the use of UNEs” and that these differences can create impairment if CLECs are limited to special access. *Id.* And, perhaps most importantly, the Court agreed that

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relegating carriers to special access created the “risk of ILEC abuses” in light of the ILECs’ incentives to set special access rates as high as possible. *Id.*

As explained more fully below, the Commission should conclude that the existence of special access affords no basis to deny requesting carriers access to loops and transport UNEs where impairment otherwise exists. The Commission can do so either by holding that the existence of special access is irrelevant to impairment determinations for landline services due to administrability issues or by finding that special access tariffs do not guarantee the rate levels and performance standards necessary to eliminate impairment.

Finally, while the Court treated special access as irrelevant to impairment determinations for local services, it stated that it had to be considered in making these determinations for long distance services because these services (like wireless services) are provided in a market that is today vibrantly competitive. But as also explained below, long distance services are different from wireless services in a fundamental respect. In wireless markets, firms have a long history in profitably providing service using special access, and the absence of price squeezes reflects the unique structural characteristics of that market. By contrast, the Bells had, until recently, been excluded from long distance markets; thus, enterprise long distance services had been competitive only because all competitors obtained high capacity last mile facilities at special access rates and none had the ability to effect price squeezes. Now that the Bells have entered enterprise long distance markets, all this has changed. With respect to all new business and all competitive bidding for contract renewals, there is exactly the same risk of price squeeze and other Bell abuses for all long distance services as there is for local services. Thus, impairment exists for all landline services, local and long distance alike.

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For these and other reasons, relegating competitive carriers to tariffed special access services would have crippling consequences for these carriers, competition, and the Commission alike. It would require competitive carriers to face radically different “risks and opportunities” that would impair their ability to offer competing landline local and long distance services and insure that competition could not “flourish[.]” *USTA II*, 359 F.3d at 576. Similarly, attempts to determine the viability of retail competitive carrier service under the incumbents’ special access tariffs would pose severe “administrability” issues for the Commission. *Id.* In such cases, the Commission would not only have to assess whether competitive carriers have opportunities to compete on the merits given the incumbents’ existing special access rates (and performance levels) under hundreds of tariffs in light of the incumbents’ prevailing retail rates – which often are not publicly known. The Commission would also have the further impossible task of monitoring the competitive significance of the incumbents’ changes to these rates, because the incumbents would have both the ability and incentive to implement anticompetitive pricing in the dynamic enterprise marketplace. As *USTA II* indicated, these factors abundantly support re-adoption of the rule that treats the availability of tariffed special access services as irrelevant to unbundling determinations – with a possible exception only for CMRS services, for which the incumbents’ incentives and ability to abuse their control over high capacity loops and transport may be very different and appears to be *de minimis*.

A. *USTA II* Authorized Re-adoption Of The Rule That Treats Special Access Services As Irrelevant To Impairment Determinations For Landline Services.

Since 1996, the Commission has treated the availability of special access as irrelevant to unbundling determinations. In *USTA II*, the Court of Appeals did *not* find any problem with this rule when it reviewed the Commission’s loop and transport rules insofar as they authorized competitors to obtain these facilities as UNEs and use them to provide landline local exchange

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services. *See* 359 F.3d at 573-75. But the Court held that the rule had not been adequately justified and was overbroad insofar as it applies to wireless carriers, who had long obtained the incidental transport facilities used in their networks under special access tariffs, because it found that the record overwhelmingly indicated that wireless services were and would continue to be “vibrantly competitive” whether or not transport was available as a UNE. The Court thus vacated the rule that treated special access tariffs as irrelevant to impairment determinations, noting that the rule had not been adequately justified.

The Commission’s primary justification for this rule has been its view that the incumbents would otherwise have the unilateral authority to evade the Act’s standards that require UNEs be made available at cost-based rates. *USTA II* held that this justification was legally impermissible. 359 F.3d at 575-77. At the same time, however, the Court recognized that there are other grounds on which this categorical rule may be justified – “factors such as administrability, risk of ILEC abuse, and the like” – and it stated that the Commission may in fact re-adopt the rule on remand if it makes certain findings that are applicable either to all services that use UNEs or to specific categories of such services. *Id.*

In particular, the court acknowledged that, “given the ILECs’ incentives to set the tariff [special access] price as high as possible and the vagaries of determining when that price gets so high that the ‘impairment’ threshold has been crossed,” a rule that allowed incumbents to avoid unbundling by offering a UNE at a tariffed rate “might raise real administrability issues,” and that these “complications might in principle support a blanket rule treating the availability of tariffed services as irrelevant to impairment.” *Id.* at 576. But it noted that the Commission’s prior rule had not been justified on this ground. It also stated that the justification seemingly would not justify giving access rights to wireless carriers, for it noted that Commission had not

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“claim[ed]” that incumbents would be able to hike special access rates for wireless carriers alone. *Id.* The Court further noted that tariffed services “present different opportunities and risks for the requesting carrier than the use of UNEs” and acknowledged that that this fact too may justify findings of impairment in certain cases, even when facilities are available from incumbents outside of § 251(c)(3). *Id.*

The Commission should retain its prior rule here, because each of the three justifications the Court specifically identified is present. Thus, with the possible exception only of the unique market for wireless services, the Commission should readopt its categorical rule that treats the availability of special access as irrelevant to impairment/unbundling determinations under § 251(d)(2).

First, there is a substantial “risk of ILEC abuse” if competitive carriers are left with access only to special access services for the limited levels of facilities they can buy as UNEs. *See infra* subpart B.1. This risk exists because the Bells’ special access prices are far above economic cost. Thus, even if the Bells could not raise prices any further – and they most certainly can in the areas where they have received pricing flexibility – they can use this existing artificial access cost advantage at any time to foreclose competition by lowering retail rates to prices their rivals cannot match.

And although a showing of actual abuse is not required under *USTA II*, AT&T demonstrates below that the Bells today are in fact *already undertaking* price squeezes for a broad array of enterprise services, such as private line and Frame Relay services. Indeed, the impact of the Bells’ artificial access cost advantage is so stark that AT&T has effectively abandoned providing several enterprise local services. The Bells have also provided special access services upon discriminatory terms and used that discrimination to win customers away

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from more efficient rivals. Given that the Bells have *already* abused their access charge monopolies to foreclose competition in a broad array of markets, this provides indisputable evidence that the “risk of ILEC abuse” is exceedingly high and that special access is not a meaningful substitute for UNEs.

Second, special access services “present different opportunities and risks for the requesting carrier than the use of UNEs.” *See infra* subpart B.2. Before offering a local or long distance service, a competitive carrier must have a reasonable assurance that it will be able to obtain critical access inputs at rates that will enable it to charge retail prices that are low enough to be attractive to customers in competition with other likely offers, and high enough to cover the costs of the last mile facilities and the other inputs into the finished retail services. Given that provision of services in enterprise markets requires a carrier to (i) incur fixed and sunk costs and (ii) commit to provide existing, modified, and new services to a customer at a fixed rate for several years, entry decisions cannot naively assume that existing rates for special access will continue in perpetuity. Rather, the carrier must also consider the rates for last mile access that will prevail in the years after entry as well as the performance standards that will apply to requests for existing and new facilities.

Given competitive carriers’ need for reasonable and stable access rates, special access poses radically different risks and opportunities and is significantly inferior to UNEs as a vehicle for serving enterprise customers. The incumbents enjoy substantial market power over the DSn-level facilities (below the capacity thresholds) necessary to serve the vast majority of enterprise customers. Incumbents also have the ability to raise their rates for special access services in many of the most important markets. Indeed, the Bells have already raised special access rates to levels that are foreclosing competition for a broad array of services to enterprise and other

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business customers. Further, even where today's special access rates may permit entry, the Bells have the ability not only to raise those rates tomorrow to levels that block rivals from competing for new (or renewal) business but also to cause their rivals to incur losses under fixed-price contracts with existing customers. Because these rivals already know that the Bells have this ability, they are often deterred from entering in the first place. In contrast, the Bells have no direct control over UNE prices. UNE rates are generally established for a multi-year period and can only be increased if the Bell can demonstrate to an independent state regulatory commission that economic costs have in fact increased. UNEs thus provide competitive carriers with the rate stability that they need to make rational entry decisions.

Special access also provides lower quality service compared to UNEs. Carriers do not compete on the basis of price alone, but also on the quality of the services they offer. While state commissions have adopted "performance measures" that are designed to detect and punish discriminatory UNE provisioning by the Bells, the Commission has adopted no such metrics for special access. Thus, if carriers are remitted to special access, the Bells can also foreclose competition by simply providing their rivals with inferior quality special access service.

Lastly, special access carries different "risks" than UNEs. In order to obtain the level of discounts touted by the Bells, a carrier must subscribe to a Bell "overlay" tariff. These tariffs, however, contain exclusionary "lock-up" provisions that require a carrier to maintain the vast majority of its traffic with the Bell for years. These poison pills severely discourage facilities-based competition because they make it impossible for competitive carriers to shift their traffic from the Bells' networks either to their own facilities or those of alternative providers. They also increase the risks of entry by imposing severe penalties on carriers that cannot maintain the demand that they anticipated. On the other hand, UNEs can be purchased at reasonable rates on

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a month-to-month basis and without shortfall penalties. Thus, unlike special access, they can serve as a “bridge” mechanism that enables competitors “to enter the market gradually, building a customer base up to the level where its own investment would be profitable.” *USTA I*, 290 F.3d at 424; *id.* (“the more widespread the availability of elements that can be more efficiently provided by the incumbent. . . the quicker competitors will set about providing the other elements”).

Third, reflecting the availability of special access services in an impairment analysis “raise[s] real administrability issues.” *See infra* subpart B.3. Even if the Commission could determine that existing special access rates did not create the “risk” of price squeezes – which it certainly cannot given the overwhelming evidence that the Bells are price squeezing competitors *today* – the Bells have the ability tomorrow to raise those rates, lower service quality, or impose other exclusionary non-price terms. Thus, to the extent that the Commission would even consider treating special access service as a potential substitute for UNEs, it would have to constantly monitor the industry to determine whether the Bells were seeking to leverage their artificial access advantage and make UNEs available where they were taking such advantage. This is simply not a workable regime. Furthermore, as the Bells technical capabilities expand, the range of high capacity long distance services that they will enlarge – as will the scope of their price squeezes.

There is an enormous range of services at issue, all with different cost characteristics. These range from (1) services (*e.g.*, point-to-point private line) for which special access represents virtually all the costs of service and where a price squeeze exists, *a fortiori*, if loops and transport are unavailable as UNEs to (2) services where special access is a lower (but still significant) percentage of total costs. And even if a static analysis were permissible, the

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Commission would have to make service-by-service determinations. Such reviews would require that the Commission not only determine the rates being charged for special access, but also the costs of all the other inputs into the specific retail service. In order to make such assessments, the Commission would have to start by determining which (of the numerous) tariffs applied and the price the competitor would qualify for under the applicable tariff. For some services, special access would likely be purchased under both state and federal tariffs. And for multi-location customers, multiple tariffs would also have to be reviewed. The next step would require a review of the Bells' retail rates, but the Bells do not publicly disclose many of their offers, and their "standard" offers for standard services are contained in voluminous pricing guidebooks that require an analysis comparable to that needed to calculate their special access prices. In contrast, allowing competitors to buy cost-based UNEs significantly reduces the Bells' ability to initiate price squeezes⁴¹ and avoids these administrative difficulties.

B. The "Risk Of ILEC Abuses," "Different Opportunities And Risks" Inherent In The Use Of Special Access And UNEs, And "Administrability" Concerns Require Re-adoption Of The Commission's Historic Rule Treating Special Access As Irrelevant To Unbundling Determinations.

Each of the three justifications *USTA II* identified as legitimate support for the Commission's historic disregard of special access in making impairment determinations is abundantly present in the real world. Thus, there is substantial justification for re-adopting the Commission's historic rule that ignores the availability of special access services in assessing impairment.

⁴¹ It is also noteworthy that the rates charged for UNEs are to be based on the incumbents' long run incremental costs. In a competitive marketplace, however, the incumbents' retail pricing decisions are based on their short-run incremental costs, which, as we show in Part II *supra*, are virtually always lower than competitors' incremental costs, and in some cases may be zero.

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1. Forcing Competitors To Purchase Above-Cost Special Access Services Creates A Substantial “Risk” That The Bells Will Foreclose Competition By Executing Predatory Price Squeezes.

As *USTA II* recognized, the Bells have a strong incentive to set special access prices high. 359 F.3d at 576. Notably, the Court did not require the Commission find to a *certainty* that the Bells could act on that incentive and raise rates to levels that would foreclose meaningful competition before it may re-adopt its rule that ignores special access in assessing impairment (although AT&T provides evidence below that satisfies that higher standard). Rather, the Court stated that the Commission may re-adopt its rule to the extent it finds that there is a “risk” that the Bells can effect such market power abuses. In this regard, the D.C. Circuit has also made clear that the existence of *some* competition is “not enough” to demonstrate that price squeezes are not occurring. *See also WorldCom Inc. v. FCC*, 308 F.3d 1, 10 (D.C. Cir. 2002) (“After all, classic price squeeze cases have never turned on a finding that competition by the input purchasing firm was *absolutely* precluded.”) (emphasis in original). There is simply no doubt that a “risk of ILEC abuse” clearly exists for both local and long distance wireline services.

High-capacity loop and transmission facilities are an essential component in providing retail services to enterprise customers. A carrier cannot offer either local or long distance service unless it can connect its network with the actual premises where its customers’ traffic is originated and terminated. For services provided over high-capacity facilities, the cost of these facilities is typically the largest component of the overall cost of service. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 22. Indeed, in many instances, the cost of this access accounts for the majority of the overall costs of service. *Id.*; *see also* UBS, *How Access Charges Determine Winners and Losers in Telecom Services*, at 22 (April 2, 2004) (“In many instances, the special access circuits required to connect the end user to the IXC network represent the majority of the total cost of the circuit. That is, more than 50% of the total cost of a frame relay

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drop or private line circuit is represented by the cost of the last mile that the IXC's must pay to the ILEC's.”).

Accordingly, when access prices are above their economic costs, the Bell can use the cost differential between what its rivals pay for the use of the pertinent facilities and their (much) lower economic costs for those same facilities to gain a significant competitive advantage in the provision of retail services. Selwyn Dec. ¶¶ 66, 73-79. Indeed, the Commission has long recognized that a Bell can raise rivals’ costs and foreclose competition by extracting from the rivals a greater margin for access than the Bell earns on its own integrated end-user services, thereby deterring efficient competitive supply of the retail service. *See LEC Classification Order* ¶ 83 (a local exchange carrier “can profitably raise and sustain prices above competitive levels and thereby exercise market power . . . by increasing its rivals’ costs or by restricting its rivals’ output through the carrier’s control of an essential input, such as access to bottleneck facilities, that its rivals need to offer their services”); *MCI-WorldCom Merger Order* ¶ 81 (absent regulation, a carrier that controls a “bottleneck” input can foreclose competition in the downstream market for services that rely upon that input); *MCI-BT Merger Order* ¶¶ 39-40; *Michigan 271 Order* ¶ 40 (same).

The Commission identified this very problem in its *Access Reform Order*. There, it explained, “[t]he incumbent LEC could [create a price squeeze] by raising the price of interstate access services to all interexchange carriers, which would cause the competing in-region carriers to either raise their retail rates to maintain their profit margins or to attempt to maintain their market share by not raising their prices to reflect the increase in access charges.” *Access Reform Order* ¶ 277. Alternatively, it recognized that “the incumbent LEC could also set its in-region, interexchange prices at or below its access prices. Its competitors would then be faced with the

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choice of lowering their retail rates for interexchange services, thereby reducing their profit margins, or maintaining their retail rates at the higher price and risk losing market share.” *Id.*

The extent to which the Bells’ special access rates are well above economic cost today can be readily quantified. Special access services are provided over the same facilities and are functionally equivalent to high-capacity loop and transport UNEs set under the Commission’s forward-looking, economic cost methodology. *Accord Local Competition Order* ¶ 679 (“We believe that our adoption of a forward-looking cost-based pricing methodology . . . establish[es] prices . . . based on costs similar to those incurred by the incumbents.”). Thus, in his accompanying declaration, Joseph Stith compares the Bells’ tariffed interstate special access rates, on a state-by-state basis, with the rates for functionally equivalent cost-based UNEs. Mr. Stith conducts this analysis both for the Bells’ “month-to-month” special access rates and its “discounted” offerings.⁴² Mr. Stith also conducts this analysis with respect to the Bells’ special access rates in MSAs where they have obtained full “pricing flexibility” and in areas where they continue to be governed by price caps.

In almost all instances, the Bells’ special access rates are well in excess of TELRIC levels. For example, Verizon North’s “discounted” DS1 special access rates are *129% higher* than comparable UNE rates and SBC-Ameritech’s “discounted” DS1 special access rates are *171% percent higher* than comparable UNE rates. Stith Dec. ¶ 17. Indeed, even the Bells’ “price capped” special access rates are in most instances significantly higher than TELRIC levels. *Id.* ¶¶ 17-18. Other carriers have likewise demonstrated that prevailing special access

⁴² Mr. Stith’s analysis is conservative, because the Bells’ “discount” tariffs include severe shortfall penalties that can effectively raise the cost of obtaining special access under these “discounts.” Mr. Stith, however, does not reflect the potential impact of such penalties in his analysis.

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rates are well above the prices that they currently pay for comparable UNE facilities. *See Ex Parte* Letter from Michael Pryor, representing NuVox, to Marlene Dortch, FCC, (Jennings Dec., Tables 2-4 (filed Aug. 19, 2004)) (showing that DS1 special access rates offered by BellSouth are well in excess of EELs rates NuVox currently pays).⁴³ Ultimately, these facts are so obvious that the Bells concede them. *See Ex Parte* Letter from Edwin Shimizu, Verizon, to Marlene Dortch, Att 1 (filed WC Docket 04-313, Sep. 28, 2004) (stating that Verizon’s average price for a DS1 UNE is \$168 per month, but that the average price for a DS1 sold as a special access service is \$247 per month).

The gulf between Bell special access prices and underlying economic costs can also be seen in how the Bells charge their retail customers for access. Specifically, in their retail offerings, the Bells often price the “access” component of the service separately from the other components of the service (such as long haul transport, ports and permanent virtual circuits). Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 45. In many cases, the rates Bells charge their retail customers for access are a small fraction of what they charge wholesale customers for comparable functionality, *id.*, even where the wholesale customers purchase much larger quantities of access and present a much lower credit risk. This strongly suggests that the Bells’

⁴³ In the past, the Bells have attempted to justify the disparity between their special access rates and forward-looking costs by attacking the Commission’s TELRIC rules, claiming that since special access rates are “competitively disciplined,” TELRIC must be considered the problem. In fact, it is the Bells’ argument that is flawed. The Supreme Court has flatly rejected the incumbents’ criticisms of TELRIC and has upheld the established forward-looking cost estimation methodology as a fully valid and compensatory method of calculating the incumbents’ true economic costs. *See Verizon*, 535 U.S. at 509-10. Indeed, TELRIC is, if anything, *overly* compensatory, given that costs must be calculated on the basis of existing wire center locations and given the inevitable regulatory lag in TELRIC price adjustments. *Id.* at 506.

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true economic costs are much lower than the rates that they currently charge competitors for special access services.

Under these conditions, there is an extremely high “risk” of anticompetitive Bell conduct. Because special access rates are already well above economic cost, the Bells clearly have the ability to price squeeze their rivals. And even if they cannot raise their special access rates any higher, they can lower their retail rates at any time to levels that simply do not permit competition.

In the past, the Commission relied on regulatory “safeguards” to ameliorate these concerns, but even these protections have been eliminated. *Access Charge Reform Order* ¶¶ 278-80; *LEC Classification Order* ¶¶ 126-130. The Commission has allowed the § 272 obligations for many of the Bells to sunset and the remaining Bells will soon be free of those requirements. The Commission has also eliminated the OI&M obligations it imposed on the Bells, despite recognizing that this would enhance the Bells’ ability to engage in non-price discrimination. *OI&M Order* ¶ 24. Moreover, as Dr. Selwyn explains, it is quite easy for the Bells to evade § 272’s imputation requirement by designing discriminatory special access tariffs. Selwyn Dec. ¶ 75, n.68. Indeed, the Bells’ OPPs clearly favor their own long distance affiliates, by allowing them to earn greater discounts than their traffic would otherwise justify relative to larger customers.

Likewise, the Commission previously relied on price cap regulation to prevent price discrimination by the Bells, *LEC Classification Order* ¶ 126; *Access Charge Reform Order* ¶¶ 278-80, but that regulation has effectively been gutted by the *Pricing Flexibility Order*. Thus, the only protection remaining against price squeezes is the availability of cost-based UNEs – the very protection that the Bells seek to eliminate in this proceeding. *See Access Reform Order*

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¶ 280 (“[S]o long as an incumbent LEC is required to provide unbundled network elements quickly, at economic cost, and in adequate quantities, an attempted price squeeze seems likely to induce substantial additional entry [through network elements] in local markets.”); *LEC Classification Order* ¶ 130 (“We agree with commenters that assert that the risk of the BOCs engaging in a price squeeze will be greatly reduced when interLATA competitors gain the ability of competing carriers to purchase access to the BOCs’ networks at or near cost.”).

The Bells do not deny any of these economic and regulatory facts. Instead, they claim that, as an empirical matter, competitive carriers are vigorously competing for both local and long distance customers using special access services. 7/02/04 Verizon Letter at 17-19. Thus, they say, this evidence conclusively establishes that competition is “flourishing” despite the fact that competitors are using special access services.

This claim cannot be taken seriously. *First*, the Bells’ position rests on an undocumented and unverifiable “study” that claims competitive carriers are generally using special access services rather than UNEs. *Id.* at 17-19; Verses Dec. ¶ 49. To the extent that Verizon has disclosed its analysis, Verizon’s methodology has been shown to be flawed. *Ex Parte* Letter from Christopher T. McKee, XO, to Marlene Dortch, at 16 (filed August 11, 2004) (“8/11/04 XO Letter”). As XO explains, Verizon ignored the *conversion* of special access circuits to UNEs. *Id.* As a result, Verizon grossly overstates the actual amount to which competitors are using special access rather than UNEs.

The Bells’ empirical claim is also directly rebutted by the sworn evidence offered by competitive carriers that rely heavily on UNEs to provide service, which demonstrates the devastating impact that paying above-cost special access rates would have on their ability to offer local service. These carriers predominantly rely on UNEs to provide service and could not

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profitably offer service if they were forced to convert to special access service. For example, NuVox currently purchases DS1 EELs to provide voice and data services to small and medium sized businesses. Although NuVox purchases some special access, the vast majority of its services are provided using UNEs. *See* Jennings Dec. ¶ 9 (attached to *Ex Parte* Letter from Michael Pryor, NuVox, to Marlene Dortch (filed Aug. 19, 2004)). According to NuVox’s calculations, if it were required to use special access instead of cost-based UNEs, that would “increase [its] network costs by 53 percent on average and would result in earnings (“EBIDTA”) per customer going from positive to negative.” *Id.* ¶ 12. Similarly, Z-Tel has provided sworn evidence that forcing it to purchase special access rather than UNEs devastated the economics of its planned new VoIP offering for medium-sized businesses. Declaration of Robert Curtis ¶¶ 37-38 (filed in DC Circuit No. 00-1012, May 24, 2004); *see also* 8/11/04 XO Letter at 18 (explaining that elimination of EELs would make “competitive entry uneconomic” for XO).

Second, the fact that carriers are currently providing local services does not mean that it is profitable to do so. For example, Verizon makes much of Time Warner Telecom’s statement that it relies primarily on special access to serve customers (where it does not deploy its own facilities). 7/02/04 Verizon Letter at 17. Time Warner Telecom, however, has never earned a profit, 8/11/04 XO Letter at 17, which likely explains why it has come forward with evidence that it too requires UNEs in order to profitably serve customers, *see Ex Parte* Letter from Thomas Jones, TWT, to Marlene Dortch, Att. at 1-2 (Sept. 8, 2004). More broadly, since 2001, 48 CLECs have sought bankruptcy protection under Chapter 11 or been shut down or liquidated. Selwyn Dec. ¶¶ 21, 30-31. And those that have emerged have suffered tens of billions of dollars in economic loss. *Id.*

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Third, in all events, the relevant issue is not how many customers are currently being served with special access, but how many more are *not* being served because it is uneconomic to do so using special access. With respect to AT&T, that is a substantial number. As explained in greater detail below, AT&T has been forced to use special access services instead of UNEs to provide finished retail services because of the Bells' historic resistance to providing EELs, their "no facilities" policies, and the lock-up provisions contained in their special access tariffs that require AT&T to maintain the vast majority of its traffic as special access. Despite its best efforts to offer customers the full range of local voice and data services that they demand, AT&T has been forced to effectively cease providing several local services altogether, because it is simply not profitable to do so in light of the Bells' existing special access rates and their retail pricing practices. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶¶ 98-103.

In particular, AT&T has effectively abandoned providing some types of local private line and Ethernet services. *Id.* ¶¶ 101-03. Critically, in each instance, AT&T has a strong incentive to provide the service if it could do so. *Id.* ¶¶ 98-99. AT&T would not only earn profits for its shareholders, but it would increase the overall utilization of its local network infrastructure, thereby increasing its economy of scale and lowering overall costs. *Id.* ¶ 98. Notwithstanding these strong incentives, AT&T has effectively been forced to restrict its offers for these services, because they are simply uneconomic for AT&T in light of the Bells' special access rates.

In addition, AT&T has developed analysis that compares the cost it incurs for the leased access input component of core enterprise services with the Bells' retail rates for those services. As these detailed studies show, competition for these services is simply not possible, because the Bells' special access rates *alone* are higher than their retail rates for many data services that they offer. *Id.* ¶¶ 78-97. Such evidence *a fortiori* establishes a price squeeze. *WorldCom Inc.*, 308

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F.3d at 10 (“After all, classic price squeeze cases have never turned on a finding that competition by the input purchasing firm was absolutely *precluded*.”) (emphasis in original).

AT&T’s analyses were developed as follows. First, AT&T maintains a database that records the actual access prices it pays the incumbents. *Id.* ¶ 73. AT&T can determine from this database the average access price it pays in a particular region or state. *Id.* These prices include all applicable discounts that AT&T receives based on term and “lock-up” commitments. *Id.* ¶ 75. AT&T’s experts then use these data to make a direct determination of whether the Bells’ special access rates permit meaningful competition for typical service arrangements. They compare publicly available Bell retail rates for a range of representative services provided to businesses with the average access costs that an efficient provider would incur in providing those services.

Beyond ignoring all of the costs incurred in providing retail service other than last-mile access, this analysis is also extremely conservative because AT&T, the nation’s largest special access customer, typically obtains the largest discounts available. *Id.* ¶ 76. In addition, AT&T’s analysis does not reflect the economic impact of having to agree to exclusionary terms to obtain these discounts. AT&T’s estimates of retail prices is likewise overstated and conservative for these purposes; AT&T relies on the Bells’ “standard” retail prices contained in their public guidelines. *Id.* ¶ 70. The Bells, however, typically offer discounts or other incentives when competing for the retail customers they consider to be the most desirable. Selwyn Dec. ¶¶ 89-90. But because the details underlying these offers are not publicly available, it may very well be that a specific deal that a Bell has offered a particular end user customer is a price squeeze even when its “list price” offer may not be. *Brooke Group*, 509 U.S. at 236 (relevant prices for

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antitrust purposes are “transactional prices” and not “list prices”); *In re Baby Food Antitrust Litigation*, 166 F.3d 112, 128 (3d Cir. 1999).

The numbers tell the story. For example, AT&T’s experts undertook a detailed examination of Verizon interstate private line offering at both the DS1 and DS3 level. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶¶ 79-86. This analysis shows that AT&T cannot possibly compete with Verizon’s prices for a typical private line service configuration. In all of the configurations analyzed, AT&T’s average access cost alone is far in excess of Verizon’s retail price for the *entire* service and is also well over the price that Verizon lists for the retail access component of its private line offering. *Id.* Given this fact, there can be no debate about whether the special access component accounts for AT&T’s inability to meet Verizon’s retail price.

The Bells are also engaging in price squeezes for Frame Relay services. For example, as shown in the Benway-Holleron-King-Lesher-Mullan-Swift Declaration, AT&T undertook a detailed examination of a representative Frame Relay arrangement in the SBC territories, at both the DS1 and DS3 level. *Id.* ¶¶ 90-96. That analysis shows that AT&T cannot match SBC’s retail prices where it must rely on special access to compete. For the DS1 arrangement, SBC’s retail price is *lower* than the price that AT&T, on average, must pay SBC region-wide for special access alone. *Id.* ¶¶ 90-93. The same results obtained for the DS3 analysis. *Id.* ¶¶ 94-96. AT&T also analyzed the overall price squeeze impact in the SBC region by examining the average access cost across SBC’s territory, and analyzed the specific impact in the Ameritech and SWBT regions, where AT&T has lost significant frame relay business. *Id.* ¶¶ 92-96.

In short, the Bells utterly fail to establish that competitive carriers are – or could – “thrive” by purchasing special access services. To the contrary, the evidence shows (i) that

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many competitive carriers rely predominantly on UNEs to provide service and would not be able to offer services profitably if forced to use special access; (ii) that those that rely on special access services and are losing money; and (iii) that those that rely on special access have been forced to use special access services and thus been subject to competition-foreclosing price squeezes. To say the least, these conditions unambiguously demonstrate that there is a huge “risk of ILEC abuses” if competitive carriers are forced to compete using special access.

2. Special Access Tariffs “Present Different Opportunities And Risks For The Requesting Carrier Than The Use Of UNEs.”

As discussed above, the Bells have the clear ability to price squeeze competitive carriers that rely on special access services. The reason for this is that the Bells’ special access prices are already set well above their economic costs. The Commission has long agreed that, by setting prices for essential access functionality above economic cost, a Bell gains an “artificial advantage [that] may allow the BOC affiliate to win customers even though a competing carrier may be a more efficient provider in serving the customer.” *Non-Accounting Safeguards Order* ¶ 12. This is true even for those special access rates governed by price caps, because those rates were initially set on the basis of historical costs that did not reflect the fact that costs have been declining rapidly.

The 1996 Act adopts a cost standard for network element rates because Congress understood that opportunities to obtain loops and transport at ILEC tariffed rates can never be sufficient to allow competition to develop. Prior to 1984, competitive IXC’s had the right to obtain what is now known as special access by tariff, but there was overwhelming evidence that the Bell System had impeded competition by effecting what amounted to price squeezes by charging excessive prices for special access services, by reducing prices for retail long distance services, and by constantly shifting from one anticompetitive stratagem to another. *United States*

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v. *AT&T Co.*, 524 F. Supp. 1331 (D.D.C. 1982); *United States v. AT&T Co.*, 552 F. Supp. 131 (D.D.C. 1982), *aff'd*, 460 U.S. 1001 (1983). Because of (i) the array of types of facilities that can be used in providing special access service, (ii) the infinite array of pricing plans that can be devised, (iii) the variety of ways in which services can be provisioned, (iv) the fact that tariffed rates vary from locale to locale under both interstate and intrastate tariffs and that the incumbents can also unilaterally alter the rates, terms, and conditions for their special access services by filing modifications to their tariffs, and (v) the low margins that competitive carriers can realize on downstream services, it was determined that the Commission should prevent incumbents from offering wholesale special access and retail services under terms that foreclose or impair competition. Thus, first in the MFJ and then in § 271 of the Act, the Bells were barred from providing long distance services, which assured that they lacked the incentive and ability to price services in ways that foreclose competition and that all IXC's would receive the same prices for the same special access services. *SBC Commun. Inc. v. FCC*, 138 F.3d 410, 412 (D.C. Cir. 1998) (“divestiture was called for, in large part, because it was thought ‘that a corporation that enjoyed a monopoly on local calls would ineluctably leverage that bottleneck control in the interexchange (long distance) market.’”) (quoting *United States v. Western Elec. Co.*, 969 F.2d 1231, 1238 (D.C.Cir.1992)). The Bells were allowed to enter long distance only when they fully implemented the statutory requirements of cost-based access to network elements designated by the Commission. *See* 47 U.S.C. § 271(c)(2)(B).

For this reason, the D.C. Circuit’s concern about the different “risks and opportunities” of special access versus UNEs can only be overcome if it can be shown that the incumbents’ ability to manipulate prices and quality is effectively constrained by competition or regulation. Since neither exist with respect to special access services, those services cannot be considered as an

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adequate substitute for UNEs. Thus, the Commission should re-adopt its blanket rule against consideration of special access tariffs both on the basis that relegating competitors to special access creates a severe “risk of ILEC abuses” and because use of special access imposes substantially greater risks on competitive carriers that deter the likelihood of entry and competition.

The Bells Have The Demonstrated Ability To Hike Special Access Rates. Given the magnitude of access costs relative to the total costs of providing retail services, a carrier’s decision as to whether to enter a particular market or provide service to a particular customer depends critically upon the availability of reasonable and stable rates for this functionality. Most obviously, at the time entry would occur, such rates must allow the carrier to profitably offer service that it seeks to offer – *i.e.*, the costs of access functionality combined with all of the other service-related costs must be less than the retail rate it charges its customers. And the carrier must also have a reasonable assurance that its last mile costs will be stable for the foreseeable future.

This is so for two basic reasons. First, as the Commission has recognized, enterprise services are ordinarily provided pursuant to contracts that obligate the carrier to provide retail services at a fixed price and for a several year period. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 25. Thus, if the charges for the ILEC inputs to the carrier’s retail service increase over the term of the contract, it can suddenly find itself providing services at a loss. *Id.* Second, even when a carrier can lease some of the last-mile facilities it needs to provide retail services to enterprise customers, these services still require additional sunk expenditures. *Id.* ¶ 24. For example, certain managed services require the carrier to invest in designing a customized network. ATM services require the carrier to have or invest in additional packet switches and

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associated facilities. *Id.* And for multi-location customers, the carrier may wish to lease inputs from the Bells for some locations and incur sunk costs in deploying its own facilities to serve some of the customer's high-demand/close-by locations. Rational entry decisions thus require a reasonable expectation that input costs (including ILEC charges) will remain at levels that allow the carrier to recover the costs of these sunk investments over a multi-year period. *See* Robert D. Willig, Determining "Impairment" using the Horizontal Merger Guidelines' Entry Analysis at 3-4 (attached to *Ex Parte* Letter from C. Frederick Beckner III, AT&T, to Marlene Dortch, FCC (CC Docket Nos. 01-338 *et al.*, Nov. 14, 2002)) (entry decisions are not made on the basis of current prices and costs, but those that will prevail after entry); *Ex Parte* Letter from Hon. Robert Bork, AT&T, to Chairman Michael Powell (CC Docket Nos. 01-338 *et al.*, Jan. 10, 2003), at 4-5 (same).

Special access service, however, provides much more limited rate stability than UNEs. That is because the Commission has largely deregulated special access services. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶¶ 27-33. In the many key markets where the Bells have obtained "Phase II" relief under the *Pricing Flexibility Order*, *see Triennial Review Order* ¶ 397 n.1235, they have the authority to raise special access rates on a single day's notice.

And, because of the lack of alternatives and barriers to entry in those markets, there is no competitive constraint preventing the Bells from raising special access rates.⁴⁴ Indeed, it is widely recognized that the "Regional Bell Companies dominate the special access market." Frost & Sullivan, *U.S. Private Line Market, June 2004* at 15. As described above in Part II, the

⁴⁴ To the extent that the *USTA II* court appeared to believe that the ILECs' ability to raise special access rates is constrained by the resale obligation of § 251(c)(4), *see* 359 F.3d at 575, that is clearly mistaken. The Commission has expressly held that special access is a wholesale service not subject to resale discounts under § 251(c)(4). *Local Competition Order* ¶ 873.

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Bells have special access market power for one simple reason: there are no alternatives to the Bells for DS_n-level transmission facilities on the vast majority of routes where carriers need such service. And it is specious to contend that supracompetitive Bell prices would attract additional facilities-based competition. It is simply not economic for a carrier to incur the enormous fixed and sunk costs of deploying bypass facilities to serve locations and routes that require only a limited number of DS₃s of capacity.

In fact, the Bells no longer seriously dispute their dominance over special access services. Indeed, they now acknowledge that competitive alternatives are the exception, not the norm. As Dr. Selwyn shows in his accompanying affidavit, the “fiber maps” the Bells provided to the Commission demonstrate that even in the most dense urban areas, competitive carriers have been able to deploy alternative fiber to only a small fraction of the buildings served by Bell special access facilities.⁴⁵

For example, in the financial district of San Francisco, competitive carriers serve 68 buildings with their own facilities, but 719 buildings via special access. Selwyn Dec. ¶ 47, Table 3. The results are the same in other major markets dominated by the Bells. *Id.* ¶¶ 36-49. Indeed, the Bells concede that competitive carriers are even unable to serve the preponderance of buildings that sit immediately adjacent to the handful of buildings where competitors have deployed fiber transport. *Id.*

Nor does the Commission have to guess about the Bells’ ability to hike special access rates, because they have repeatedly done so where the Commission has deregulated their rates. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 33. Shortly after receiving Phase II pricing

⁴⁵ In this regard, the Bell maps do not show buildings served by carriers leasing UNEs.

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flexibility, BellSouth and Verizon each increased their rates for DS1 service throughout *every* Phase II MSA in their regions – even in the central business districts of major cities such as New York, Boston, and Atlanta. *Id.* BellSouth also raised its monthly rates for DS3 services in all of its Phase II MSAs throughout its region. *Id.* Shortly thereafter, Qwest followed suit, raising its rates for DS1 service in every Phase II MSA in its region. *Id.* This is, of course, the exact opposite of what one would expect to see in competitive markets, because the per unit costs of providing special access have substantially *decreased*, due to factors such as technological improvements in fiber optic electronics, scale economies and substantially increased demand for special access services. AT&T Reply Comments, Ordoover-Willig Reply Dec. ¶ 3 (filed in RM No. 10593, Jan. 23, 2003).

The result of these steep price increases is predictable: the rates in MSAs where the Bells have obtained full “Phase II” pricing flexibility are almost always much *higher* than those in MSAs where they have *not* (yet) gained such relief. Stith Dec. ¶ 19; *Ex Parte* Letter from Thomas Jones, TWT, to Marlene Dortch, Atts. 2-3 (filed CC Docket No. 01-338, Sep. 8, 2004). For example, Verizon North’s DS1 special access rates in Phase II MSAs are on average over 30% higher than rates in its non-pricing flexibility MSAs, and its DS3 special access rates in pricing flexibility MSAs are over 11% higher than those in non-pricing flexibility MSAs. Stith Dec. ¶ 19. Similarly, BellSouth charges, on average, between 15% to 29% more for DS1 and DS3 special access in pricing flexibility MSAs than in non-pricing flexibility areas. *Id.*

This cannot be explained as “rate rationalization” given that the MSAs where relief has been granted are typically the most urban areas in the country. The economic costs in these more urban areas are most likely to be *lower* than in other areas, because of the Bells’ ability to concentrate relatively greater demand on relatively shorter routes. Thus, the Bells’ pricing

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structure is the *antithesis* of what one would expect to see in competitive markets – their rates are higher where their costs are lower.

The Bells’ attempts to cloak their price increases in pro-competitive terms range from the meritless to the ludicrous. In a recent filing, the Bells’ renewed their shopworn claim that special access revenue per line have actually declined, on a DS0 equivalent basis. 9/28/04 Verizon Letter, Att. 3. But the Bells’ own data actually tell a quite different story. Revenue per line did decline between 1996 and 2001, but these declines should not be surprising, because at that time, the Bells were still governed by price caps and an X-Factor. Further, the Bells did not begin obtaining pricing flexibility in significant numbers of markets until 2002, and thus there is no way these alleged revenue decreases can be attributable to the effects of “deregulation.”

Equally important, the Bells focus on revenue per line on a DS0 equivalent basis and ignore its relationship to average “investment” and average “expense” per line during the same period. Although the Bells’ revenue per DS0 equivalent line declined slightly over this period, as AT&T has demonstrated, average expense per DS0 equivalent line dropped by an even greater amount. AT&T Reply Comments, at 29 (filed in RM No. 10593, Jan. 23, 2002). Accordingly, the Bells’ net return, on a DS0 equivalent basis, increased enormously.

In all events, calculating revenue per line on a DS0 equivalent basis is fundamentally misleading, because it ignores the fact that the Bells’ effective price per DS0 equivalent circuit varies between different kinds of services. In other words, the decline in revenue per DS0 equivalent line is likely due principally to a changing mix of services. Specifically, the Bells’ higher capacity services – *i.e.*, DS3 and OCn services – likely grew at a faster rate over this period, and because the Bells’ effective price per DS0 equivalent is lower for these services, this changing mix of services would manifest itself as a declining revenue per line when calculated

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on a DS0 equivalent basis. The more appropriate comparison, however, is to compare rates for the same service, and as AT&T has demonstrated, the Bells' Phase II rates are uniformly higher than their non-Phase II rates.

This is underscored by the fact that while the Bells' rates have increased, their costs have unquestionably decreased over the same period. Again, in competitive markets, a decline in costs should lead to *lower* prices. To be sure, competitive carriers can achieve some "rate stability" when purchasing special access. But, as explained in the Benway *et al.* declaration, the rate stability that can be achieved is limited and requires a competitive carrier to agree to other terms that otherwise substantially increase its business "risk." Specifically, rate stability is only available on "committed" special access demand. *Id.* ¶ 39. However, the combination of severe shortfall/termination penalties and fluctuating and declining demand make it economically impossible for a competitive carrier to commit all of its traffic to these plans. *Id.* This is particularly true in connection with the longest term plans that offer the best rates; with the aggressive entry of the Bells into long distance markets existing competitive carriers can expect to see rising customer churn, declining market share and declining demand. As a result, they must purchase substantial volumes that are tied directly to the "month-to-month" rates. *Id.*

Thus, even if a carrier could achieve full "rate stability" only by agreeing to take on enormous downside business risk that make special access services substantially inferior to UNEs as a way of serving customers in a competitive marketplace. *Id.* ¶¶ 39-41. Any significant decline in its demand would subject it to onerous shortfall/termination liabilities that would dramatically increase its per-unit costs. *Id.* Indeed, with respect to many plans which require a carrier to commit specific circuits, mere shifts in the distribution of its demand can

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cause it to incur shortfall and/or termination penalties. *Id.* The Bells, of course, do not have to incur these risks in order to obtain access rate stability.

In the evolving market for bundled enterprise services (including long distance), the Bells are now the principal new competitors, and they can obtain their access needs at economic costs. In this new environment, the difference in the “opportunities and risks” between special access and UNEs is stark. To the extent it is even feasible in light of the Bells’ high special access rates, entry must occur under the omnipresent threat of further special access price increases (and Bell retail price decreases) that devastate any business case that might otherwise justify another competitor’s entry decision. The Bells’ control over special access rates thus deters efficient entry.

The Bells, on the other hand, do not labor under the terms and conditions that they impose on special access subscribers. They incur no artificial shortfall penalty if their demand decreases. They incur no termination liability if a customer wishes to decrease demand at one location and increase it at another.

The conditions relating to UNE pricing are starkly different. While the Bells have the demonstrated ability and incentive to raise special access prices to competition-foreclosing levels at their whim, they cannot do the same with UNEs. Access to UNEs is available at rates set by state commissions on the basis of forward-looking economic cost. UNE rates are typically set for a multi-year period – thus providing reasonable rate stability – and cannot be increased unless the incumbent can show that its economic costs have in fact increased. On the other hand, special access rates can be (and have been) increased even where costs are declining.

The Bells Have The Demonstrated Ability To Lower Special Access Quality. There is also a substantial difference between the quality of special access and UNEs. To fulfill the

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requirements of §§ 251 and 271, state commissions required the Bells to adopt performance measures designed to detect and prevent discriminatory UNE provisioning. *See, e.g., Nevada 271 Order* ¶¶ 50-51. And in all its § 271 orders, the Commission ensured that the applicant was subject to a performance measurement and enforcement plan. *Benway-Holleron-King-Lesher-Mullan-Swift Dec.* ¶ 52. But there is no comparable regulation of special access provisioning quality. *Id.* ¶¶ 42-51. Although the Commission opened a proceeding on this subject several years ago, stating that it recognized the critical need to “expeditiously” “address[] special access performance metrics” in light of its decision to eliminate § 272 OI&M safeguards and allow the other safeguards to “sunset,” *OI&M Order* ¶ 24, it has taken no action.

The Commission’s inaction has freed the Bells to act on their incentives to provide AT&T and other rivals with patently inferior special access service quality compared to the service they provide to themselves and their retail customers. AT&T and other carriers have provided both the Commission and state regulators with detailed data showing that the Bells (i) often do not provide firm order confirmations on a timely basis, (ii) frequently miss installation commitments and (iii) take too long to repair or restore problem or trouble circuits to normal operating levels and often compromise customer service. *Benway-Holleron-King-Lesher-Mullan-Swift Dec.* ¶ 48; *see also* Petition for Rulemaking at 18-19 (filed in CC Docket No. 01-321, Oct. 29, 2001); Comments of AT&T at 13-14 (filed in CC Docket No. 01-321, Jan. 22, 2002); Comments of Focal at 4 (filed DA 00-1141, June 23, 2000). This record evidence includes both sworn testimony of anticompetitive Bell practices and hard data showing the Bells’ poor (and in many cases, declining) service quality. *Benway-Holleron-King-Lesher-Mullan-Swift Dec.* ¶ 48, 50 (attaching *Swift Dec.*, Att A (attached to Reply Comments of AT&T (filed in CC Docket No. 01-321, Feb. 12, 2002))); *Waldbaum Dec.* (attached to Reply Comments of

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AT&T (filed in CC Docket No. 01-321, Feb. 12, 2002))). The evidence further shows that the Bells provide competitive carriers substantially worse performance than they provide their own retail affiliates. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 48 (attaching Direct Testimony of Eileen Halloran, at 9-13 (filed in Mass. DTE Docket No. 01-34, Feb. 6, 2002))).

State commissions that have investigated the Bells' special access performance have reached the same conclusion. The New York PSC determined that "Verizon's provision of Special Services is below the threshold of acceptable quality." Opinion and Order Modifying Special Services Guidelines for Verizon New York Inc., Conforming Tariff, and Requiring Additional Performance Reporting, NY PSC Case 00-C-2501, at 5 (June 15, 2001). The Colorado PUC found that "AT&T has experienced regular, frequent, widespread, and ongoing delays in obtaining access." *AT&T v. US WEST*, Decision No. R00-128, CPUC Docket No. 99-4405, at II.D, F. G (Colo. PUC Feb. 7, 2000). The Colorado PUC further found that this poor performance was discriminatory: "US WEST has provisioned DS1s and DS0s to AT&T on a wholesale basis after a longer interval than it provided those same services to other wholesale customers." *Id.* And the Minnesota PUC held that there is considerable evidence "that the quality of US WEST's wholesale access service" is discriminatory and began an investigation as to whether it can remedy that situation, *Complaint of AT&T Commun.*, 2000 Minn. PUC LEXIS 53, 34 (Aug. 15, 2000) – an inquiry that Qwest has fought tooth and nail, *see Qwest Corp. v. Scott*, 380 F.3d 367 (8th Cir. 2004).

The evidence also makes clear that the Bells' poor provisioning is intentional, not the result of simple neglect. AT&T quite often must wait weeks – or months – to get a response to an order for special access service. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 50. In many instances, when AT&T's order has been delayed in this manner, it has learned from the

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customer that the Bell approached it directly and offered to provide the necessary service, often in a shorter time. *Id.* Despite AT&T’s best efforts, these anticompetitive practices continue to this day. *Id.*

The fact that the SBC companies have been willing to include performance standards in their special access tariffs does not demonstrate that they lack the ability to provide rivals with inferior performance. Given the Bells’ lack of competition, it is unsurprising that most of the Bells have not even been willing to put into place performance measures and the ones agreed to by SBC are patently inadequate. *Id.* ¶ 51.⁴⁶ Thus, when purchasing special access services, competitive carriers get no assurance that they will obtain those services at parity with the Bell.

Ultimately, the proof is in the pudding. Despite the existence of these “voluntary” performance measures, AT&T continues to receive patently discriminatory service from the Bells. *Id.* ¶ 48.

And these differences in the quality of special access and UNEs are of enormous competitive significance. Just as enterprise customers prefer low prices, they also prefer high quality service. *Id.* ¶ 47. If AT&T cannot match a Bell’s service quality, it is at an enormous competitive disadvantage. *Id.* Thus, “[u]nlawful discriminatory preferences in the quality of the service . . . as a practical matter, can have the same effect as charging unlawfully discriminatory prices.” *Non-Accounting Safeguards Order* ¶ 12; *see id.* (“If a BOC charged the same rate to its affiliate for a higher quality access service than the BOC charged to unaffiliated entities for a lower quality service . . . the BOC could effectively create [a] ‘price squeeze.’”); *LEC*

⁴⁶ SBC’s MVP measures are also deficient because the MVP is an exclusionary lock-up tariff. *See infra* Part III.C. Thus, SBC offers (weak) performance measures *only* to carriers that agree to (1) restrict their use of special access alternatives from competitive carriers or their own facilities and (2) restrict their purchase of UNEs.

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Classification Order ¶ 111 (“[T]here are various ways in which a BOC could attempt to discriminate against unaffiliated interLATA carriers, such as through poorer quality interconnection arrangements or unnecessary delays in satisfying its competitors' requests to connect to the BOC's network. . . . [This gives a BOC] the ability to raise prices by restricting its own output upon entry or shortly thereafter.”).

The Bells' Special Access Tariffs Contain Poison Pills Designed To Prevent Competition.

In contending that special access is a meaningful substitute for UNEs, the Bells have pointed to the “discounted” rates that they offer under their OPPs. 7/2/04 Verizon Letter at 19. They make no claim that competition can “flourish” under the Bells’ month-to-month tariffed rates. Nor could they, given the huge gap between the month-to-month tariff rates and comparable UNE rates. *See* Stith Dec. ¶¶ 17-18. The Bells’ OPPs, however, contain poison pills that are designed to block carriers that subscribe to these tariffed services from using alternatives to compete. Thus, even if the OPPs provided the same rates as UNEs, these additional exclusionary conditions greatly increase the “risk” of purchasing special access relative to UNEs.

First, to get the discounts touted by the Bells, *see* 7/2/04 Verizon Letter at 19, competitive carriers must not only adhere to the conditions discussed above with respect to the Bells’ rate stability plans, but also the conditions contained in the Bells’ “overlay” OPP tariffs that provide additional discounts. A carrier, however, cannot obtain the Bells’ most-heavily “discounted” OPP rates simply to purchase a particular circuit. Because of that fact, Bell special access service is not *available* as a substitute to UNEs in any meaningful sense under the OPPs.

As the D.C. Circuit recognized, the impairment analysis must be conducted on the basis of relevant markets with similar characteristics. *USTA II*, 359 F.3d at 575. Moreover, the Commission cannot infer impairment (or lack of impairment) from the extent of competition in

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markets with very different characteristics.⁴⁷ But to get the best prices – *i.e.*, the ones that the Bells claim will enable competition – a subscriber must be willing to lock up virtually *all* of its traffic and forgo both self-deployment and third party supply. *See supra* Part III.C. Thus, even in those limited instances where one could imagine a circumstance in which a competitive carrier might be able to use special access in lieu of the limited facilities that may be available as UNEs, that carrier can only obtain special access at a somewhat lower (but still exorbitant) price by agreeing to *give up purchasing UNEs*, as well as the opportunity to self-deploy facilities in instances where special access is patently inadequate to support competitive entry. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 59.

These OPPs also impose severe shortfall penalties on carriers that fail to meet the minimum traffic requirements. *Id.* ¶ 60. They are analogous to “take or pay” contracts in which the “take” amount is based on the carrier’s historical special access demand. This dramatically increases the “risks” of special access. *USTA II*, 359 F.3d at 576. A carrier that serves retail customers using special access is subject to potentially enormous shortfall penalties if its retail business does not materialize as anticipated, or if drops over time. This gives the Bells a powerful incentive to target rivals that use special access, because by winning business away from that carrier it wins twice: first, it gains the customer’s retail business, and second, it still retains its wholesale revenues, because the shortfall penalties require the rival to “pay” for the demand it does not “take.” Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 60. State commissions have not permitted the Bells to impose any comparable penalties for UNEs, which are available at reasonable month-to-month rates. *Id.* ¶ 61.

⁴⁷ For example, the existence of competitive OCn facilities at a building says nothing about another competitor’s ability to deploy DSn-level facilities at the same building.

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3. It Would Be Administratively Impossible For The Commission To Reflect The Impact Of Above-Cost Special Access Pricing In Its Impairment Analysis.

As shown above, the Bells have in fact already been using special access to price squeeze rivals. This alone supports the re-adoption of the blanket rule treating special access as irrelevant to impairment determinations. But even if the Commission could assure itself that the Bells were not undertaking price squeezes today, that does not remotely establish they lack this ability going forward. So long as there are structural conditions that allow the Bells to undertake price squeezes – *i.e.*, effective deregulation of their special access rates and lack of price-constraining competition – an impairment rule that reflects the potential availability of special access would require the Commission constantly to monitor the Bells activity to ensure that they were not acting on their incentive to price squeeze. Such a rule is simply not workable, because there is no way for the Commission to keep up with the myriad ways in which the Bells can price squeeze their rivals.

History provides a powerful example of the Bells' ability to change their rate structure overnight from one that allows competition to flourish to one that forecloses competition altogether. After SBC was granted authority to provide in-region long distance service, it began providing mass market long distance service and charged rates that were generally competitive with prevailing long distance carriers' prices. Lieberman-Panerali Dec. ¶ 17. Dissatisfied with the share it was able to gain from such competitive pricing, SBC decided to tilt the competitive playing field dramatically. In March, 2003, SBC began offering pricing plans in which long distance service was provided at rates that were well-below the lowest prevailing long distance rates. *Id.* ¶¶ 17-18.

AT&T simply could not profitably match those rates, because of the cost disadvantages resulting from the access charges it had to pay SBC for originating and/or terminating long

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distance calls. *Id.* ¶¶ 18-19. Given that switched access costs represent a substantial percentage of the cost of the overall costs of long distance services, SBC's retail prices were simply too low to allow AT&T to match them and still recover all of its other costs to provide long distance.⁴⁸

Id. In contrast, the reason that SBC could profitably offer such rates was precisely because it has a monopoly share of local service customers throughout each state where it offers long distance service, and because the SBC enterprise does not incur the "switched access" and other charges SBC imposes on its long distance competitors to originate or terminate calls to these customers.

Id. ¶¶ 7-19.⁴⁹ Once SBC undertook this new pricing strategy, it quickly became the dominant provider of long distance services in its territories, whereas AT&T – which had previously held the largest share of the residential long distance market in SBC territories before this change in SBC's pricing strategy – has now ceased marketing residential long distance services.

For these reasons, any rule that considered special access tariffs as relevant to the impairment inquiry would necessarily require the Commission to continuously evaluate and monitor market conditions to determine whether prevailing wholesale and retail rates are

⁴⁸ Because the Bells' generally have provisioned their voice long distance services simply by reselling high competitive IXC-provided services, it is unlikely that SBC enjoys efficiency advantages outside of the access portion of the service.

⁴⁹ Critically, even to the extent that competitive carriers can obtain originating access at economic cost by using "UNE-P" to provide local service to customers, SBC still enjoys an artificial cost advantage in offering long distance services. Competitive carriers ordinarily have to pay terminating access for their customer's calls because it is very infrequent that one of their local customers makes a long distance call to another local customer of that carrier. Lieberman-Panerali Dec. ¶ 14. On the other hand, it is quite often the case that for SBC – with its monopoly customer base across 13 states – to have one of its customers call another of its customers. *Id.* In such circumstances, SBC effectively avoids above-cost terminating access charges, instead incurring only the lower economic cost.

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sufficient to allow meaningful competition absent access to UNEs. Such an inquiry is not administratively feasible.

Specifically, in order to find that the availability of special access eliminates impairment sufficiently so that cost-based access to UNEs is unnecessary, the Commission would have to continuously monitor market conditions to (1) assess thousands of actual (or potential) wholesale special access rates, (2) assess actual or potential ILEC retail rates for the full range of retail services provided to enterprise customers and (3) predict whether there could be the equivalent of a price squeeze that would foreclose entry (or require market exit) by efficient competitors if they were remitted to tariffed special access. Selwyn Dec. ¶¶ 80-98. Even if such a national inquiry were only conducted on a retrospective basis reflecting the conditions that currently exist in every market today, this would be an incredibly daunting task. But it would almost certainly be impossible going forward, because it would require the Commission to constantly monitor and assess the myriad ways in which incumbents could unilaterally change either wholesale or retail rates (or combinations of both) in the future to effect squeezes or similar anticompetitive actions.

First, as explained in the accompanying declaration of Dr. Selwyn, AT&T and other carriers provide numerous retail services that use special access as an input. AT&T, for example, uses special access to provide private line, local voice, long distance voice, ATM, Frame Relay, and Virtual Private Network services and many other data services. Selwyn Dec. ¶¶ 66-67. However, each of these services relies on special access as an input in different ways. For each and every such service offered by AT&T – and every other competitive and long distance carrier – the Commission would need to determine whether the carrier offering

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competing services could profitably offer those services at the wholesale rates the ILEC charges those competitors. *Id.* ¶ 90.

This would be a huge undertaking. At a minimum, it would require the Commission to determine the special access prices that each incumbent charges and compare them to the incumbent's retail prices for the array of services that it provides using special access as an input. *Id.* ¶¶ 90-98. Such a review would in turn require the examination of hundreds of federal and state tariffs with respect to all of the various services at issue, because the incumbents provide interstate special access, intrastate special access, interstate retail, and intrastate retail services. *Id.*

Moreover, the special access costs incurred in providing a particular service necessarily depend on the specific terms and conditions of that service. Thus, the Commission could not make generic comparisons of the "price" for special access with the "price" for the retail service; instead it would have to make such calculations for each particular service and customer location. For example, special access services are distance sensitive. *Id.* ¶ 93. Thus, the Commission would need to determine the "length" of special access services used in the retail service at issue in order to determine the underlying cost of special access. *Id.* Further complicating this task is the fact that special access rates vary by geography. *Id.* Thus, for each service at issue, the Commission must examine the incumbent's special access tariffs to determine the appropriate rate that applies to services in that specific location. *Id.* ¶ 94. And, of course, for multi-location customers, this process must be repeated for each customer location (which may involve multiple incumbents with different tariff structures). *Id.*

And that is just the easy part of the analysis. Although the presence of Bell special access rates that are higher than comparable retail rates conclusively establishes a price squeeze, a price

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squeeze can obviously exist even where the Bell's retail rates are above its wholesale rates for special access that is used is a competitor's finished retail service. That is because for most retail services, special access is only one of several inputs necessary to provide the service. *Id.* ¶ 95. Thus, the Bell can still foreclose competition if it sets a retail price that is above the price of its special access, but not high enough that competitors can recover their other efficient costs of providing the retail service. *See Triennial Review Order* ¶¶ 83, 90.

Thus, if the Commission were to incorporate an investigation of special access into its impairment analysis, it would have to examine the other costs that a carrier incurs to provide local and long distance services. This examination would necessarily include the cost of other network facilities used to provide finished retail services. *Selwyn Dec.* ¶¶ 90-98. For example, long distance services provided to enterprise customers require not only special access facilities, but also long haul network facilities (such as the required transport, switching and signaling equipment). *Id.* Similarly, the costs of facilities used to provide, for example, Frame Relay functionality must be included in any reasoned price squeeze analysis for those services as well. *Id.*

Providing finished retail services, however, requires more than just network facilities. It also requires expenditures on employees to plan, operate, and maintain those facilities. *Id.* ¶ 96. It further requires marketing and sales costs, as well as costs for customer care, and billing. *Id.* All of these "back office" costs are actual costs incurred by any efficient carrier and must therefore be reflected in any price squeeze analysis.

The difficulties of making such assessments would not be resolved by permitting competitive carriers to file complaints seeking after-the-fact-damages. *Selwyn Dec.* ¶ 98. The informational demands attendant to price squeeze determinations would place a substantial

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burden on competitive carriers, and many competitive carriers simply lack the resources to pursue such claims. And critically, data supporting such claims is often unavailable, because the Bells' retail rates for enterprise services are often not published. Thus, competitive carriers would often lack even the ability to determine whether the Bell's retail price was one that it could have profitably matched given the access charges it was paying. Finally, and most importantly, the purpose of the 1996 Act is to create a regulatory structure that enables competition – not merely to create after-the-fact causes of action for price squeezes that were already illegal under pre-existing antitrust laws. Indeed, by definition, under such a regime, a competitive carrier would be denied access to a UNE where impairment exists and have lost the opportunity to compete meaningfully.

Moreover, this inquiry would be required even if the Commission were to find – notwithstanding the overwhelming evidence to the contrary – that the Bells have not yet acted on their incentives to price squeeze. There are many reasons why the absence of a price squeeze today is quite irrelevant to whether a Bell has incentive and ability to undertake such anticompetitive conduct in the future. For example, to the extent that a competitive carrier is providing service to an existing customer under a contract, the Bell cannot “win” that customer's business until the contract expires. It is only at that point that the Bell needs to offer retail rates that an equally efficient rival could not match because of the rival's access cost disadvantage. Thus, the absence of a price squeeze today may reflect nothing more than the fact that the Bell is waiting for the appropriate time to act.

The Bells may also be curtailing their behavior for strategic considerations. They certainly know that if they were to price squeeze too nakedly today it would substantially undermine their attempts to eliminate access to cost-based UNEs. The value to the Bells of the

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near-term elimination of UNEs altogether is most likely greater than the “cost” of delaying a broader price squeeze campaign for a few more months.

A Bell’s incentives to price squeeze also turn on its assessment of the risks and benefits of the current market situation. To the extent competitors are using special access for “niche” services, a Bell might calculate that it is economically better off keeping its retail prices “high” and also earning above-cost revenues from the special access it sells to rivals than by lowering retail rates and driving the rival out. Or the Bell may not yet have the technical capability to provide the same type of retail service as its rivals. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 65. But as those specific market conditions change, the Bell’s incentives will also radically change.

Finally, while there are some existing economic and regulatory constraints on the Bells’ ability to price squeeze, these constraints are disappearing. Unlike residential markets, where the Bells could enter by simply “flipping a switch,” the Bells do not yet have the ability to offer the full suite of services that enterprise customers desire. *Id.* ¶ 65. Thus, although the Bells’ special access prices are anticompetitive raising rivals’ costs of offering enterprise services that rely on special access as an input, the Bells do not yet have the ability to create a complete price squeeze for these services. But as they build on their success in price squeezing rivals in the business services markets that they have now entered, they will shortly gain the ability to offer any additional services that they do not have the capability of providing today. *Id.* At that time, they will have the same incentive and ability to price squeeze these other services as they do for the services that they currently offer – and where the evidence clearly shows that they are already undertaking concerted price squeeze campaigns.

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Moreover, although current regulatory constraints on the Bells' market power are weak, some do exist. Most notably, the Bells have not achieved full pricing flexibility in all of their MSAs. Thus, in those markets their special access rates are governed by the Commission's price cap regulations. As Mr. Stith shows, the rates in those areas are generally below the Bells' rates in non-price cap areas. Stith Dec. ¶ 19. But as the Bells increasingly gain pricing flexibility relief, their ability to price squeeze will only grow. Likewise, as § 272 obligations sunset, there will be fewer constraints on the Bells' ability to undertake price squeezes and non-price discrimination.

In addition, the very elimination of cost-based UNEs will necessarily *increase* the Bells' ability to raise special access rates. Although the limited availability of cost-based UNEs did not provide a complete check on the incumbents' special access prices, it provided some constraint on their ability to fully exploit their special access monopolies. *Accord Access Reform Order* ¶ 280; *LEC Classification Order* ¶ 126. For example, carriers that can satisfy the Commission's "use restrictions" could use UNEs to either self-provide exchange access or even offer exchange access to third parties. This alternative to Bell special access puts some pressure on the Bells to moderate special access rates in order to retain business. Correlatively, any reduction of competitive carriers' right to obtain cost-based UNEs gives the Bells greater ability to raise special access prices. Thus, the very act of eliminating UNEs increases the likelihood that the Bells can price squeeze in the future.

Recent actions confirm this economic common sense. In the wake of *USTA II*'s vacatur of the Commission's transport rules, the Bells have substantially increased their special access rates. These actions underscore the Bells' ability to raise prices and effect a price squeeze. And

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they also demonstrate that the mere fact that a Bell may not yet have imposed a price squeeze is not probative of whether it could do so if UNE loop and transport facilities were eliminated.

For example, on August 16, 2004, Qwest filed rate increases for its special access services subject to pricing flexibility of between 9% and 94% with an average rate increase of 27%. Selwyn Dec. ¶ 83; Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 13. This is Qwest's third major rate hike in less than two years, and the second in the last six months. Selwyn Dec. ¶ 83; Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 13.

BellSouth has made even more dramatic changes to its special access rate structure. On June 23, 2004, shortly after the *USTA II* decision and the collapse of carriers' attempts to negotiate "commercial" access agreements, BellSouth entirely eliminated its tariff that provided volume-based discounts for large special access purchasers. *Id.* ¶ 36. As a result, carriers that are not grandfathered under any existing plan have no ability to obtain a volume-based discount in the *entire* BellSouth region. *Id.*

In sum, any reliance on special access as a substitute for cost-based UNEs carries with it a responsibility to ensure that the Bells do not foreclose competition by price squeezing their rivals. And this is a task that the Commission cannot feasibly undertake. Instead, consistent with sound economics, the Commission should hold that the availability of special access does not eliminate the impairment faced by competitive carriers that are denied access to cost-based UNEs.

C. "Existing" Wireless And Long Distance Competition Does Not Require The Commission To Consider Special Access In Determining Impairment For Facilities Used To Provide Wireline Services.

USTA II held that, for wireless and long distance services, the Commission must at least consider the relationship between special access and impairment, subject to the justifications for not including special access in its final impairment rules discussed above. 359 F.3d at 575-76,

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592. The court's rationale was that these markets have an established history of competition in which competitors used special access. On the other hand, the court did not mention this consideration at all in its discussion of the Bells' challenge to the Commission's unbundling of loop and transport facilities (indeed, as explained in Part I, *USTA II upheld* the Commission's loop rules). This strongly suggests that such an inquiry is not required for local wireline services, which have no history of competition using special access and have traditionally have been, and continue to be, dominated by the Bells. *See, e.g., IDC, U.S. ATM Service Forecast and Analysis, 2001 – 2006* (June 2002) at 24 (RBOCs have 96.9% share of local ATM services); *IDC, U.S. Frame Relay Services Forecast and Analysis, 2001-2006* (Apr. 2002) at 25 (RBOCs have 90.3% share of local Frame Relay services); *Frost & Sullivan, U.S. Wholesale ATM and Frame Relay Markets* (2002) at 37 (RBOCs have 95.4% of combined local ATM/Frame Relay Services Markets); *see also* Selwyn Dec., Att. 3 (listing numerous competitive carriers that have declared bankruptcy since 2001).

In all events, the Court's discussion of unbundling in the context of wireless and interexchange services does not call into question the Commission's findings that competitive carriers are impaired without access to certain limited transmission UNEs or support any "use restriction" of such UNEs with regard to long distance services. The fact that CMRS competition might be flourishing even though CMRS carriers typically use special access as an input to their *wireless* services does not remotely suggest that competitive carriers would be able to profitably offer *wireline* services if they were relegated to special access services rather than the limited UNEs allowed in the *Triennial Review Order*. The Bells have much weaker incentives and ability to undertake price squeezes in wireless markets. Moreover, the existing levels of competition in long distance services using special access are simply a reflection of the

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fact that, until recently, *all* the major long distance competitors were *required* to purchase special access to serve business customers. Thus, none had the ability to impair competition from their rivals. That situation is radically changed. The Bells have now aggressively entered the enterprise long distance market, and as shown above they have both the ability and incentive to price squeeze rivals that are forced to compete using special access. Indeed, they have already begun to do so.

1. Competition In The CMRS Market Is Substantially Different From Competition In The Wireline Market And Does Not Provide A Basis For Eliminating UNEs For Wireline Services.

The fact that wireless competition may have flourished using special access says nothing about wireline carriers' ability to use special access services to compete meaningfully with the Bells. There are numerous reasons why the Bells' ability and incentive to use their access cost advantages are attenuated in the context of wireless services.

Foremost, there is a significant difference in the relative impacts of the costs of special access in wireless and wireline services. Selwyn Dec. ¶¶ 102-103. Quite obviously, the Bells' ability to price squeeze competitors that use special access diminishes if special access represents only a small fraction of the total costs of the service. As Dr. Selwyn shows, special access is a significant portion of the cost of the retail services wireline carriers offer to business customers. *Id.* ¶¶ 102-103, 104. Indeed, in the specific price squeeze examples identified by AT&T, special access accounts for the majority of the total costs of the service. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 22.

In contrast, wireless services use special access in a more limited way – a link between the carrier's cell site and the PSTN. Selwyn Dec. ¶ 102. Thus, wireless carriers do not lease loops distribution from incumbents. Rather, they lease only the equivalent of loop feeder and the interoffice transport necessary to interconnect their mobile service switching offices among each

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other and with the incumbents' wireline networks. Both of these pieces of transport are shared by multiple users. As a result, special access represents only a tiny fraction of wireless carriers' total operating costs – far below what wireline carriers incur in providing services. For example, according to AT&T Wireless' Form 10-K and Annual Report to Shareholders for 2003, it spent a total of \$198 million on special access services, representing approximately 1.28% of its \$15.5 billion in total operating costs. *Id.* To put this in context, AT&T Wireless reported SG&A expenses for 2003 of \$5.4 billion – roughly 27 times its special access outlays. On the other hand, special access reflects the majority of total operating costs for landline business services. *See, e.g.,* UBS, *How Access Charges Determine Winners and Losers in Telecom Services*, at 22 (April 2, 2004) (“In many instances, the special access circuits required to connect the end user to the IXC network represent the majority of the total cost of the circuit. That is more than 50% of the total cost of a Frame Relay drop or private line circuit is represented by the cost of the last mile that the IXCs must pay to the ILECs.”); *id.* at 27 (estimating that special access costs represent 69% of MCI's business revenues derived from services provided over these facilities).

This differential in reliance on special access has competitive significance for another reason. In order to serve a new customer, a competitive wireline carrier typically purchases transmission facilities specifically to serve that customer. Selwyn Dec. ¶ 106. In other words, the carrier's purchase of special access is *incremental* to the individual customer. *Id.* In contrast, the addition or subtraction of any particular customer does not ordinarily cause the wireless carrier to change its special access purchases necessary to serve its cell sites or to interconnect its switches. *Id.* Indeed, a wireless carrier must necessarily have some minimum quantum capacity available for each of its cell sites. *Id.* Thus, to a large degree, special access service is a *fixed* cost for wireless carriers. *Id.*

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This difference means that a special access price squeeze has a more immediate and direct competitive impact on wireline carriers than on wireless carriers. *Id.* ¶ 101. To the extent that special access costs are fixed, a price squeeze will not affect a wireless carrier's near-term pricing decisions, *Id.*, and the wireless carrier can still maintain prices that fully recover short run costs.⁵⁰ *Id.* On the other hand, where special access costs are marginal with respect to serving new customers, as is the case for wireline carriers, the impact of such pricing has an immediate effect on the carrier's pricing and entry decisions. *Id.* No rational carrier will charge retail prices that are below its short run costs. *Id.*

Not only do the Bells have less ability to foreclose rival CMRS providers, they also have less incentive to do so. First, the Bells have only limited incentives to impose a price squeeze in wireless markets because of the nature of their ownership interests in the wireless providers. Unlike their wireline operations, the Bells' wireless operations are joint ventures. Verizon owns only 55% of Verizon Wireless, while Vodafone owns the remaining 45%. Cingular is jointly owned by BellSouth and SBC, and they are acquiring AT&T Wireless, the largest independent wireless operator. Qwest merely resells Sprint PCS service. This means that the costs of a price squeeze (*i.e.*, reduction of special access profits) are fully borne by the Bell but the benefits of a price squeeze (*i.e.*, the eventual ability to raise wireless prices) are shared by other parties.

There is also less likelihood of "recoupment" in the wireless context than the wireline context. A price squeeze, even while profitable, can require sacrifice of short-term profits for a longer term gain. However, because the major competitors in the wireless market are the Bells

⁵⁰ This is, of course, not to say that a carrier can price indefinitely without respect to fixed costs, but only that the carrier is still better off in the short run by pricing above its short run costs even if that does not allow recovery of its long run costs.

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themselves (as well as Sprint, which is the largest non-RBOC ILEC), a Bell that undertakes a price squeeze has little chance of so weakening its rivals that it stands to gain monopoly power. In contrast, in local wireline markets, the Bells have clear monopolies – especially for the facilities used to provide special access services – and they are in a much stronger financial position than their competitors. And as AT&T’s decision to stop marketing long distance residential markets shows, Bell price discrimination clearly has the potential to weaken competition irreversibly in the long distance market as well.

Finally, the Bells’ incentives to price squeeze in the wireless market is diminished by the fact that the Bells themselves compete head-to-head with each other. If one Bell should attempt to price squeeze the others in its operating territories, it could find itself subjected to the same treatment in their base territories. Sprint is also an incumbent and can retaliate against an SBC, BellSouth or Verizon price squeeze. This threat of “mutually assured destruction” significantly diminishes these entities’ incentives to engage in a predatory price squeeze. In stark contrast, the Bells generally do not compete with each other for wireline services.

2. Existing Long Distance Competition Provides No Basis For Eliminating UNEs For Wireline Service Providers.

The Bells also claim that UNEs are not necessary to ensure that competition in long distance markets will flourish. *See* 7/2/04 Verizon Letter at 26 (citing *USTA II*, 359 F.3d at 590). The Bells make no attempt to show that the long distance market is structurally competitive to the extent that IXCs are relegated to special access. Instead, they contend that UNEs are unnecessary to ensure that long distance competition will “flourish” because competitive IXCs continue to have the largest market shares even though they generally serve customers using special access. *Cf. id.* at 27. This is economic nonsense.

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The Bells' current market share in enterprise markets does not establish the existence of "competition" in those markets. *Capital Cities/ABC, Inc. v. FCC*, 29 F.3d 309, 315 (7th Cir. 1994). See also *United States v. Baker Hughes, Inc.*, 908 F.2d 981, 986 (D.C. Cir. 1990). The Bells (and GTE) were historically precluded by law from providing long distance services. Because IXCs generally did not have their own local networks, above-cost special access – while a drag on the nation's economy – did not distort the competitive playing field. Each IXC had to pay the same rate to access to a Bell's local network.

Those conditions have radically changed. Now, the Bells (and GTE, which merged with Verizon) have full authority to participate in the long distance market. And while the static market shares they have achieved to date might not ordinarily be viewed as indicating dominance, that market share information provides no support for the Bells' assertions in this regard. First, the Bells' existing enterprise market share reflects an unprecedented ability to gain customers in a short period of time. And it also necessarily reflects the limited time that the Bells have been permitted to compete in that market.

An important feature of the enterprise market is that large enterprise customers take service under multi-year term contracts. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 25. This structural factor has prevented the Bells from using the substantial market power derived from their access cost advantages to acquire a dominant market share – yet. But once existing contracts expire, there will be no check on their ability to wield that power, unless competitive carriers are able to purchase UNEs in cases where they do not have sufficient scale economies to construct their own facilities.

Accordingly, current market share data are not indicative of market power. Thus, that evidence should be disregarded in favor of more probative measures. *Ball Mem'l Hosp. v.*

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Mutual Hosp. Ins., 784 F.2d 1325, 1336 (7th Cir. 1986). In these circumstances, basic economic theory demonstrates that, to the extent IXC's are forced to incur access costs that are well above those the Bells incur, competition – at least continued competition – is unlikely. See *ITTA Forbearance Order* ¶ 7 (incumbent LECs “have the ability and incentive to use their bottleneck facilities to engage in cost misallocation, unlawful discrimination, or a price squeeze against rival interexchange carriers”); *LEC Classification Order* ¶ 83 (a local exchange carrier “can profitably raise and sustain prices above competitive levels and thereby exercise market power . . . by increasing its rivals’ costs or by restricting its rivals’ output through the carrier’s control of an essential input, such as access to bottleneck facilities, that its rivals need to offer their services”). The IXC's’ vulnerability to price squeezes is particularly acute given that special access accounts for the majority of the costs of many retail service. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 22.

The Commission, however, need not rely solely on economic theory to predict what will happen to long distance competition if IXC's can only gain access to enterprise customers using special access while the Bells can do so at economic cost. Even after the 1996 Act struck down state franchise laws, IXC's were unable to compete for many “local” services that were provided to enterprise customers through the use of special access. Because of the Bells’ significant cost advantages, IXC's were simply unable to compete in these local enterprise markets, where the Bells were not barred from service. *Id.* ¶ 64. The result is that the Bells to this day continue to dominate the market for local services provided to enterprise businesses, such as local private line, and local Frame Relay and ATM service. Indeed, given the lack of access to UNEs, AT&T is restricted in its ability to offer certain local private line services and Ethernet services that are competitively priced. *Id.* ¶¶ 98-103.

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Moreover, as described above, the Bells are now engaging in these same practices to extend their dominance into adjacent long distance markets. The Bells have set retail prices for a host of long distance services at prices that no rival can match in light of their bloated access rates. *Id.* ¶¶ 72-103. Indeed, in many cases, the Bells are offering retail prices for finished end-to-end services that are *below* what they charge competitors for access. As a result, the Bells have made dramatic inroads in these markets even though they lack the same long haul network facilities that their competitors have. *See infra* Part IV. And, of course, this is due in no small part to the fact that the Bells are able to secure access to long haul facilities at highly competitive rates, in stark contrast to the monopoly prices that confront competitive carriers seeking to purchase access to the Bells' last-mile facilities. Statement of Randall Stephenson, CFO, SBC First Quarter Financial Release Conference Call (Apr. 2003) ("We have very little capital in our long distance business. We pretty much buy the long haul transport.")

For example, Verizon reported that its first quarter of 2004 "included nearly 500 Enterprise Advance sales to customers. Enterprise Advance is Verizon's initiative to connect *and extend its local networks and services to the national large-business market.*"⁵¹ Overall, Verizon touts that it has "closed" "over 2,000 opportunities . . . to date"; has "[o]ver 100 Fortune 500 customers" and "[o]ver 900 total unique customers"; and that it is "[t]argeting \$250 million in new revenue for 2004."⁵²

Similarly, in the first quarter of 2004, SBC reported that in the large-business market, it "expects approximately \$200 million in incremental revenues from its large business initiative in

⁵¹ Verizon's Investor Quarterly, Q1 (April 27, 2004) at 4 (emphasis added).

⁵² Verizon, 2nd Quarter 2004 Earnings Conference Call, Doreen Toben, Chief Financial Officer, July 27, 2004, at 20 (available at <http://investor.verizon.com/news/20040727/20040727.pdf>).

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2004.”⁵³ In the second quarter, SBC reported that in the large business market segment SBC “respond[ed] to 57 percent more bid requests in the second quarter of 2004 than in the year-earlier second quarter ... contracts won in this space have increased 34 percent from the fourth quarter of 2003 [and t]he dollar value of contracts won has increased as well, up more than 30 percent versus the second quarter of 2003.”⁵⁴

Most notable is the Bells’ success rate in winning contracts for which they bid. Verizon trumpets the fact that it has won *over a third* (68/203) of enterprise segment requests for proposals (“RFPs”) since the beginning of 2003 to which it responded and for which contracts were awarded. 7/2/04 Verizon Ex Parte, Bruno Dec. ¶ 21. And according to the Yankee Group, “[c]ombined, AT&T, MCI and Sprint lost 33 contracts and gained only 17 – a net loss of 16 contracts. On the other side of the ledger, the RBOCs achieved a net gain of 10, with SBC and Qwest leading the group of net gains.” Yankee Group, *Communications Survey Confirms IXCs Lost Enterprise Market Share in 2003* (March 19, 2004). The predominant reason was *price*. *Id.* at 2-3.

Most starkly, the Bells themselves concede that they are thriving as a direct result of their access cost advantage. SBC states that it has been winning customers by leveraging its “access cost advantage” and that “it will continue to bid aggressively for business contracts with enterprise customers that fit similar traffic patterns [*i.e.*, that have significant traffic in SBC’s region].” CIBC World Markets, *Key Takeaways from CIBC Communications and Technology Food Chain Conference*, at 3-4 (June 9, 2004); *see also* SBC Communications Analysts Meeting,

⁵³ Investor briefing (available at http://www.sbc.com/Investor/Financial/Earning_Info/docs/1Q_04_IB_FINAL.pdf).

⁵⁴ Investor briefing (July 22, 2004) (available at <http://www.sbc.com/gen/investor-relations?pid=2985>).

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Final Transcript at 14 (Nov. 13, 2003) (“[W]e believe that we have a cost advantage over AT&T, MCI and others because they buy a lot of their local access from us and or the other regional Bell companies”). Verizon notes that “[o]ur ability to succeed in the enterprise market” is based on our “big[] advantage over everybody . . . that we have access to the end user and they don’t. Almost 90% of the circuits that wholesalers get today come through us, and when you look at the relative cost of providing networks to enterprise customers, for example, the person that wins is the person that puts the most traffic on their network and in most cases, that’s us.” Statement of Lawrence Babbio, Vice Chairman and President, Verizon Fourth Quarter Financial Release Conference Call (Jan. 29, 2003).

This parallels the Bells’ behavior in consumer long distance markets. Lieberman/Panareli Dec. ¶¶ 3-30. In just a few short years, the Bells used their access charge advantage in consumer markets to go from a zero market share to clear dominance of these markets (Selwyn Dec. ¶ 88) – leading most recently to AT&T’s announcement that it will no longer compete for mass market long distance customers. Prompt Commission action to confirm that loops and transport facilities are available at cost-based rates is necessary to prevent the incumbents from fully exploiting their access charge advantages and achieving the same anticompetitive results in business markets.

In sum, competition in long distance using special access was historically possible only because the Bells (and GTE) were historically excluded from this market and therefore had neither the incentive nor ability to price squeeze long distance carriers. As a result, all competitors were on a level playing field. Since entering that market, the Bells have already used their access charge cost advantages to price squeeze their long distance competitors. And the Bells’ incentives to do so now are particularly strong in light of enterprise customers’ desire

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to purchase local and long distance services from a single provider. Absent the availability of UNEs in situations where competitors cannot obtain alternatives, the Bells will eventually be able to dominate business long distance markets in the same way they have now achieved dominance in consumer long distance markets.

This is also true for even the largest multi-location enterprise customers. Such large customers often have a wide range of locations for which they seek service. Although such customers will often have a handful of extremely high-demand locations that can justify the deployment of last-mile competitive facilities by competitive carriers, many of those locations will have much less demand. In order to provide service to all locations – as many such enterprise customers demand – a competitive carrier must have access to cost-based incumbent high-capacity facilities in order to compete effectively. Lack of such access again subjects competitive carriers to potentially debilitating price squeezes.

IV. THE COMMISSION SHOULD NOT IMPOSE USE RESTRICTIONS ON EELS AND SHOULD ELIMINATE THE EXISTING ANTICOMPETITIVE RESTRICTIONS CONTAINED IN ILEC SPECIAL ACCESS TARIFFS.

The time has come for the Commission to finally end “use restrictions” on UNEs. In addition to the unreasonable constraints that they impose on the competitive provision of local services, these restrictions deny competitive carriers access to cost-based UNEs to provide long distance services and instead require them to purchase supracompetitively-priced special access services in order to serve customers. While this situation may have been tolerable before the Bells obtained full § 271 relief, allowing it to continue will be devastating to the facilities-based competition the 1996 Act seeks to develop. When competitive carriers are forced to use above-cost dedicated facilities instead of cost-based UNEs, the Bells can win “customers even though a competing carrier may be a more efficient provider in serving the customer.” *Non-Accounting Safeguards Order* ¶ 12. Indeed, the Bells have begun to use their artificial access cost advantage

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to price squeeze their long distance rivals with devastating effect. Elimination of existing use restrictions on EELs is thus necessary to prevent Bell remonopolization of long distance markets. The Commission should also allow competitive carriers that were forced to purchase special access because of anticompetitive restrictions to EELs to convert existing special access circuits to UNEs.

The Commission's use restrictions are not just bad policy, but they are also flatly unlawful. The *USTA II* court devastated the legal basis upon which the Commission justified its use restrictions – the “qualifying services” rule. The Court held that, to the extent impairment exists, competitive carriers may use UNEs to provide *any* telecommunications service, including using UNEs solely to self-provide exchange access in connection with their long distance service. *USTA II*, 359 F.3d at 594. Thus, the Court held that the Commission could retain its service eligibility rules *only* to the extent that it conducted a “service-specific” impairment inquiry and found that carriers providing only long distance services would be not be impaired without access to high capacity loops and transport services.

No such finding can be made here. As described above in Part II, it is simply not economic to deploy high-capacity loops up to 2 DS3s per location or high-capacity transport up to 12 DS3s per route. This is the case even where carriers can use loops and dedicated transport to offer the full range of services that can be provided over them (and thus maximize the revenues that can be generated using the facilities). *A fortiori*, carriers that offer only a subset of those services, such as only long distance services, are impaired without access to loops and dedicated transport.

Simply eliminating use restrictions, however, is not sufficient to level the competitive playing field. The Bells have taken anticompetitive advantage of competitive carriers' inability

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to obtain access to loop and dedicated transport UNEs since the 1996 Act was passed by forcing carriers that have no choice but to purchase special access to agree to onerous “lock-up” terms that require them to deal exclusively with the Bells. These provisions have the obvious intent and effect of starving competitive carriers of the traffic they need to deploy bypass facilities. This in turn allows the Bells to keep demand on their network while charging supracompetitive rates. The Commission should declare these tariffs unlawful and provide a “fresh look” to allow carriers to conduct negotiations in a context where they have true alternatives to Bell special access services.

A. The Use Restrictions Imposed In The *Triennial Review Order* Can No Longer Be Maintained In The Wake Of *USTA II*.

In the *Triennial Review Order*, the Commission correctly found that competitive carriers are generally impaired without access to high capacity loops (DS1s and up to 2 DS3s per location) and high capacity transport (DS1s and up to 12 DS3s per route). Nevertheless, it adopted “use restrictions” that bar a requesting carrier from using UNEs to provide access to its own “long distance” services unless the carrier also uses them to provide “qualifying services.” The Commission held that “qualifying services” include “those telecommunications services that have been traditionally the exclusive or primary domain of incumbent LECs,” including “local exchange service, such as POTS, and access services, such as xDSL and high-capacity circuits.” *Triennial Review Order* ¶¶ 135, 140. But the Commission held that long-distance services are not qualifying services, and thus that a requesting carrier cannot obtain a UNE “exclusively to provide exchange access to itself in order to provide a retail interexchange service.” *Id.* ¶153.

To implement its “qualifying service” restriction with respect to loop-transport combinations (known as “EELs”), the Commission adopted new use restrictions (now called

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“eligibility criteria”) that were intended to separate “qualifying” from “non-qualifying” services.

Those rules allow competitors to purchase UNE EELs only if they satisfy three criteria.

First, . . . each requesting carrier must have a state certification of authority to provide local voice service. Second, . . . the requesting carrier must have at least one local number assigned to each circuit and must provide 911 or E911 capability to each circuit. Third, [the requesting carrier must satisfy] additional circuit-specific architectural safeguards⁵⁵

Triennial Review Order ¶¶ 597. As a result, the service eligibility criteria limit a competitive carrier’s ability to use an EEL to provide long distance service only to situations in which it also provides outbound local voice service (but *not* local data services and *not* local inbound services, as discussed below).

On appeal, *USTA II* struck down the Commission’s requirement that UNEs may only be used to provide “qualifying services.” 359 F.3d at 594 (“We vacate the Commission’s distinction between qualifying and non-qualifying services.”). The Court held that long distance services are “telecommunications services” within the meaning of § 251(d)(2) and that carriers may in fact use UNEs to provide such services to the extent that the element at issue otherwise meets the standards for unbundling. *Id.* at 592. Thus, the Court stated that, on remand, Commission must eliminate its “service eligibility” criteria for EELs unless the Commission is able to find make a finding of “non-impairment” for long distance services based on a service-specific inquiry. *Id.*

⁵⁵ The “architectural safeguards” require that “each circuit must terminate into a collocation governed by § 251(c)(6) at an incumbent LEC central office within the same LATA as the customer premises; each circuit must be served by an interconnection trunk in the same LATA as the customer premises served by the EEL for the meaningful exchange of local traffic, and for each 24 DS1 EELS or the equivalent, the requesting carrier must maintain at least one active DS1 local service interconnection trunk, and each circuit must be served by a Class 5 switch or other switch capable of providing local voice traffic.” *Id.*

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There is, however, no reasoned basis upon which the Commission could make the necessary finding. In the *Triennial Review Order*, the Commission concluded that carriers are impaired without access to high capacity loops (DS1s, dark fiber and up to 2 DS3s per location) and high capacity transport (DS1s, dark fiber and up to 12 DS3s per route). In so finding, the Commission analyzed whether a carrier could self-deploy facilities considering the *full range* of services – and thus revenues – that would be generated over the facility, *including* any “non-qualifying” services. *See Triennial Review Order* ¶ 388 & nn.1205-09 (collecting record support).⁵⁶ As explained above in Part II, the record evidence developed before the state commissions and engineering testimony provided by AT&T confirm the validity of the *Triennial Review Order*’s findings.

These economic facts necessarily demonstrate that carriers would also be impaired if the same facilities were used to provide *only* interexchange services. That is because the same economic considerations that lead to a finding of impairment with respect to the *full range* of services that could be offered over a facility would necessarily impair carriers that use the facility to provide only a single category of service, *i.e.*, interexchange service. *See, e.g., id.* ¶ 303. By forcing a competitive carrier to split its total demand into two pieces (one for UNEs and one for non-UNEs), its average cost per facility could only go up for both. Fea-Giovannucci Dec. ¶¶ 24-36.

⁵⁶ The fact that long distance is a “permitted” use when a carrier also uses the capacity on a UNE to provide “qualifying” services, *Triennial Review Order* ¶ 143, confirms that the Commission’s analysis was performed on an “all service” basis, including long distance. This is logical, because the cost of transmitting an electron that is used to provide long distance is no different from the cost of transmitting an electron used to provide any other service.

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Indeed, as a matter of logic, any Commission attempt to undertake a “service-by-service” impairment analysis would only result in *more* unbundling. Because “a minute is a minute” and “a circuit is a circuit,” the cost of using a transmission facility does not depend on the type of traffic it carries. Fea-Giovannucci Dec. ¶¶ 64-65. Thus, if a carrier is using UNEs to provide only a subset of the telecommunications services it provides – and thus could expect to earn only a subset of the potential revenues that could be generated by the facilities – there would be a far larger range of circumstances in which the carrier would be unable to justify investment in the high fixed and sunk costs necessary to deploy loops and transport. This is an essential feature of all “service-by-service” impairment inquiries: the scope of unbundling will always vary inversely with the scope of the services the requesting carrier “seeks to offer.”

Nor can the Commission find that the availability of above-cost special access services eliminates impairment with respect to long distance services. Although the Bells may not yet have a dominant share of long distance services in the enterprise market, this is merely a reflection of the historical facts that (i) until recently, the Bells were barred from providing long distance services and (ii) large enterprise customers typically purchase services under term contracts. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶¶ 25, 63-68, 98. Now that the Bells have been permitted to enter all the long distance markets in the nation, they have been enormously successful in a short period of time in winning customers as their contracts expire. *See infra* Part III.C.2. And now that the Bells have obtained long distance authority, the dynamics of that market have radically changed. Thus, any assessment of competition in that market must also be adjusted to reflect this reality.

As documented above in Part III.A, the driving force behind the Bells’ dramatic gains has been the Bells’ ability – and willingness – to price-squeeze IXC rivals that are forced to rely on

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special access services to provide retail services. IXCs are extremely vulnerable to this conduct, because the costs of special access often represent the majority of the overall cost of retail services provided over special access facilities, and there is little regulatory or competitive constraint on the Bells' ability to increase special access prices (or lower retail prices). *See* Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶¶ 27, 31-37. Indeed, the Bells themselves openly acknowledge that above-cost access charges give them a competitive advantage having *nothing to do with* superior efficiency, product or quality. *See* CIBC World Markets, *Key Takeways from CIBC Communications and Technology Food Chain Conference*, at 3-4 (June 9, 2004) (reporting SBC's statements that it has been winning customers by leveraging its "access cost advantage" and that "it will continue to bid aggressively for business contracts with enterprise customers that fit similar traffic patterns [*i.e.*, that have significant traffic in SBC's region]."); SBC Communications Analysts Meeting, Final Transcript at 14 (Nov. 13, 2003) ("[W]e believe that we have a cost advantage over AT&T, MCI and others because they buy a lot of their local access from us and or the other regional Bell companies"); Statement of Lawrence Babio, Vice Chairman and President, Verizon Fourth Quarter Financial Release Conference Call (Jan. 29, 2003) (Verizon notes that "[o]ur ability to succeed in the enterprise market" is based on our "big[] advantage over everybody . . . that we have access to the end user and they don't. Almost 90% of the circuits that wholesalers get today come through us, and when you look at the relative cost of providing networks to enterprise customers, for example, the person that wins is the person that puts the most traffic on their network and in most cases, that's us."). And even in those (declining) instances where a competitive IXC is currently using special access to serve a long distance customer, at the point the customer's contract expires – or

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in the case of *any* new business – the IXC is vulnerable to a debilitating Bell price squeeze if it is required to use special access to continue serving the customer.

Thus, the current use restrictions – and the related service eligibility criteria – should be completely eliminated, especially with regard to both new and renewal contracts. In those cases, there is a substantial risk that an IXC purchasing special access will be unable to win or retain the customer’s business, because it will be unable to match the price that the Bell can offer due to its unfair access cost advantage. *See supra* Part III.B. This is particularly true in the case of renewals. In many instances, the Bells recover most, if not all, of their up-front costs of a facilities build in the initial term of the access services they sell to competitive carriers. At the same time, competitive carriers get no rate reduction for the access services they purchase when they renew a special access commitment. Thus, having already recovered a significant percentage of its costs, in the second stage of the “game” (a renewal), the Bell has the ability to offer much lower rates than the competitive carrier, which must continue to pay access rates that do not reflect the fact that substantial cost recovery that has already occurred.

The Commission should also permit competitive carriers immediately to “convert” special access circuits to cost-based UNEs. *See USTA II*, 359 F.3d at 593. From an administrative standpoint, it simply makes no sense to prevent conversions, as this will necessarily require the Commission to referee numerous disputes as to whether the customer is “new” or the contract is to be renewed. The hairsplitting between new and renewal contracts and contracts is also a waste of Commission resources in light of the fact that most “existing” contracts will expire or be renegotiated over the next few years, at which time competitive carriers would be eligible to serve customers with UNEs. Thus, a ban on conversions accomplishes nothing but preserving Bell special access monopoly rents in the short run.

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B. If the Commission Retains Any Use Restrictions, It Must Eliminate Or Substantially Modify Its Eligibility Criteria.

1. The Existing Service Eligibility Criteria Are Substantially Overbroad.

Even if the Commission were to retain any use restrictions, such limitations must apply solely to the existing circuits provided to the embedded retail customer base under existing contracts. And in doing so, the Commission must, at a minimum, reform any remaining service eligibility criteria. The existing criteria are exceptionally overreaching and prevent carriers from leasing UNEs even where they are in fact being used to provide *local* services. Thus, they are arbitrary, grossly over-inclusive and contrary to the Commission’s stated goals in adopting those very criteria.

The fact that the *USTA II* court did not overturn these requirements does not mean that the Commission should retain them. The *USTA II* court expressly acknowledged – twice – that these criteria are “imperfect,” and it upheld them only on the basis of the “considerable deference” accorded to such proxies, 359 F.3d at 592-93. The Commission thus has discretion to correct these “imperfect[ions]” on remand, and it should do so in order to ensure that any remaining eligibility criteria do not prevent competitive carriers from gaining access to EELs to provide core local services. Indeed, in the *Triennial Review Order* the Commission expressly recognized that it should modify its service eligibility rules, even if they have been upheld by a court, when experience demonstrates that they can be improved. *See Triennial Review Order* ¶ 596.

The service eligibility criteria adopted in the *Triennial Review Order* to implement the now discredited “qualifying services” test for EELs require a competitive carrier to certify that (i) it has the authority to provide local voice service; (ii) at least one local number is assigned to each circuit and it can provide 911 or E911 capabilities to each circuit; and (iii) it satisfies a

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number of architectural safeguards, including the requirements that (a) the EEL terminate in a collocation arrangement, (b) the EEL is served by a local voice switch and (c) the EEL is served by interconnection trunks carrying local voice traffic. *See id.* ¶¶ 601-11. These criteria are far too restrictive to cover even their intended purpose, because they forbid competitive carriers from using UNEs to provide services that are indisputably local – and thus have nothing whatever to do with long distance services. Even more problematic is the fact that these criteria are technology-specific, and prevent any competitive carrier from using UNEs to innovate by providing new functionality. Taken in total, these rules create artificial constraints that prevent the very economic and competitive improvements the Act was intended to foster.

Specifically, as the Commission stated in the *Triennial Review Order*, the service eligibility criteria were intended to permit a competitive carrier to gain access to an EEL only where it is providing “local voice” service to that customer. *Id.* ¶ 595. But its rules do not even identify those situations accurately, because the 911 requirement effectively requires a competitive carrier to provide local *outbound* voice services. Many carriers, however, also offer local *inbound* voice services that are typically provisioned without 911 capability. In addition, AT&T has long offered a service called AT&T Digital Link, which provides local voice service to enterprise customers using its legacy interexchange switches. Such services are not necessarily served by a § 251(c)(6) collocation, and they do not typically include a 911 capability because of the technical limitations of those switches.⁵⁷ Even though these types of services are

⁵⁷ *See Ex Parte* Letter from David Lawson, AT&T, to Marlene Dortch, at 12 (filed in CC Docket No. 01-338, Feb. 12, 2003) (“2/12/2003 AT&T Letter”); *see also* AT&T Comments, Carroll-Rhodes Decl. ¶ 15 n.7 (filed in CC Docket No. 96-98, Apr. 5, 2001) (Digital Link not intended to be a primary local service offering).

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unquestionably “qualifying” – and in many cases a local voice service – the existing criteria preclude AT&T and other competitive carriers from using UNEs to provision them. Moreover, the rules ignore the integrated nature of emerging services, for which data, voice and IP traffic are combined on a single facility for purposes of network efficiency.

The Commission’s current rules also prevent access to EELs to provide other indisputably local services. For example, EELs cannot be used to provide private line services, including those used to provide local data services. Although the Commission expressly found that local private line and data services are “qualifying” services, *Triennial Review Order* ¶¶ 135, 140, the eligibility criteria effectively bar competitors from using EELs to provide them, because those services typically do not have local number assignments or 911 capabilities.

Similarly, the requirement that the competitive carrier have a certain number of “interconnection trunks” in a LATA and that the carrier provide service using a Class 5 switch excludes private line services because these services directly connect customer locations, and thus do not require traffic to be switched or exchanged between the competitive carrier and the ILEC. Significantly, such services also provide critical transport functionality now increasingly being used by enterprise customers who are migrating their voice services to new IP-based technologies that do not involve the use of circuit switches. By excluding access to UNEs to provide such private line functionality, competitive carriers are effectively relegated to competing for an ever-shrinking market.

Finally, the Commission’s service eligibility criteria deny EELs to carriers that would provide wholesale local access. Wholesale access providers typically do not have local numbers assigned to their circuits and do not provide 911 functionality. Moreover, they likely would not provide the circuits used to provide wholesale services using local voice switches or

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interconnection trunks that carry local traffic, nor do they have to be certificated to provide local voice service. The same is true of wholesale DSL providers: although they might have switches capable of providing local voice service, they typically would not have local number assignments or 911 capabilities, and likely would not have interconnection trunks carrying local voice traffic or local voice certifications.⁵⁸ All of these services are regularly provided by ILECs today. The service eligibility criteria thus arbitrarily preclude competitive carriers from using EELs to provide these “qualifying” services and artificially limit the scope of market segments in which competitive carriers may effectively compete to a narrow subset of the services that the ILECs provide.⁵⁹

2. If The Commission Does Not Eliminate Use Restrictions Altogether, It Should Modify Its Service Eligibility Criteria.

By denying competitive carriers access to EELs where they are seeking to build networks to offer local voice and data services, the Commission’s existing eligibility criteria are at war with the Commission’s core goal of fostering facilities-based competition. *See Triennial Review Order* ¶¶ 22, 70, 114, 200, 242, 448; *Local Competition Order* ¶¶ 172, 325, 635, 685. In order to justify deploying local networks, competitive carriers generally need to be able to reach

⁵⁸ *See, e.g.*, 2/12/03 AT&T Letter at 8 (local number assignment and 911 requirements would preclude access to EELs for all local data providers). Although the record in the prior proceeding made clear that local number assignment and 911 requirements would *necessarily* preclude many qualifying carriers from obtaining EELs, the Commission never even considered these objections. *See Triennial Review Order* ¶ 602.

⁵⁹ Additionally, there is no need for the Commission to adopt any “architectural safeguard” regarding the ratio of interconnection trunks to circuits purchased by competing carrier. Carriers’ interconnection agreements provide for the sizing of interconnection facilities based on specific industry defined engineering standards to ensure availability in the range of 99.5%. Therefore, the 1 to 24 interconnection trunk to circuit ratio identified in the *Triennial Review Order* is merely an arbitrary requirement that creates additional costs for competitive carriers without providing any practical benefit.

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customers spread throughout a broader geographic area than an ILEC serves out of a single central office. That, of course, means the competitive carrier must have in place an extensive transport network to connect its customers to its switch – costs the incumbents do not incur because all of the ILECs' loops terminate at their switches – and in order to be competitive in the retail market the competitive carrier transport costs per customer must be close to the ILEC's own internal cost. If, on the one hand, the competitive carrier considers building its own loop and transport facilities, the use restrictions make it impossible to justify that construction, because it cannot aggregate its demand efficiently or use UNEs to fill in gaps in its network. If, on the other hand, the competitive carrier considers using ILEC high cost special access services to provide the necessary transport functionality, the supracompetitive prices for those services force the competitive carrier's costs far above the ILEC's own costs.

The Commission cannot remedy this situation without completely eliminating its use restrictions and associated eligibility criteria.⁶⁰ But if it chooses to maintain any limitations at all, it must at least revise them to ensure that competitive carriers have the incentive to build out their local networks where feasible, as well as the ability to obtain EELs as UNEs to reach customers where it is not feasible to self-deploy. In this regard, any future service eligibility rules must also recognize that competitive networks can provide increased facilities-based competition with the Bells not only in local voice and data markets, but can also be leveraged to provide competition in the market for interexchange access services.

Critically, the overbreadth in the existing rules is not necessary to achieve workable and reliable rules. *Triennial Review Order* ¶ 595 (the Commission “focus[ed] on local voice service

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due to its verifiability”).⁶¹ There are alternative criteria that are verifiable and would eliminate IXC’s ability to obtain EELs where they have not sought to build out local networks. As such, they are far superior to the Commission’s existing criteria – which illogically and inappropriately bar competitive carriers from using to EELs to provide what are clearly local services – and should be adopted on remand.

AT&T proposes that the Commission adopt two alternative service eligibility criteria that will promote the Commission’s core goal of promoting facilities-based deployment.⁶² The first alternative would be based on the Commission’s existing service eligibility criteria. Specifically, the Commission should allow a requesting carrier to purchase an EEL when (i) it certifies that it has obtained the authorizations necessary to offer local service in the state; and (ii) the circuit terminates into a collocation arrangement at an ILEC central office in the same LATA as the customer premise served by the EEL.⁶³ To ensure that EELs are available only to carriers that

(. . . continued)

⁶⁰ In addition, the Commission should reassert its previous finding that ILECs may not impose any commingling limitations, which is essential to enable competitors to operate efficiently. *Triennial Review Order* ¶¶ 579-81.

⁶¹ The Commission’s attempt to justify a voice-focus because voice service plays a “role as the core competitive offering, either on a stand-alone or bundled basis, in direct competition to traditional incumbent LEC service,” *id.* was clearly repudiated by *USTA II*, which (i) held that UNEs could be used to offer any “telecommunications service” for which impairment exists and (ii) authorized the Commission to adopt a use restriction only to the extent that it found that impairment does not exist for the particular service at issue. 359 F.3d at 592.

⁶² Consistent with the Commission’s existing rules, a carrier should be able to obtain an EEL when it can self-certify that one of the two criteria is met. *See Triennial Review Order* ¶ 623 (“We conclude that requesting carrier self-certification to satisfy the qualifying service eligibility criteria for high-capacity EELs is the appropriate mechanism to obtain promptly the requested circuit”).

⁶³ The Commission, however, should not artificially limit the availability of EELs only to carriers that obtain access under § 251(c)(6), as its existing criteria do, but should also recognize
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have built out a local transmission network, this alternative would not be satisfied by a requesting carrier that purchases special access services to connect the collocation to the carrier's network. Instead, connectivity between those points would have to be provided by the requesting carrier itself or through another entity other than the ILEC. For the reasons explained above, the other service eligibility criteria adopted by the Commission in the *Triennial Review Order* should be eliminated and would not be included in this alternative.

The second alternative would permit a requesting carrier to obtain an EEL where it had deployed its own switch, but does not have the traffic necessary to justify building out further towards customers. For a carrier that offers service using its own switch, the carrier would be able to obtain an EEL when (i) it certifies that it has obtained the authorizations necessary to offer local service in the state; and (ii) it certifies that the EEL is used to originate or terminate traffic on a Class 5 switch or on a switch that employs other than circuit-switched technology and provides local switching functionality and that is not solely deployed for the purpose of providing long distance services. For carriers that have deployed a Class 4 switch, the carrier would be able to obtain an EEL when (i) it certifies that it has obtained the authorizations necessary to offer local service in the state; and (ii) it certifies that the EEL is used to originate or terminate traffic on the Class 4 switch and the switch is not used solely for the purpose of providing long distance services. Again, this alternative excludes carriers that seek access to EELs using its own switches without collocation to provide purely long distance services. Indeed, any time a competitive carrier has satisfied these criteria, it will necessarily have made a

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that facilities-based carriers sometimes purchase – and have already purchased – collocation out of special access tariffs as well.

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substantial commitment to local service, including taking such actions as obtaining certification, putting interconnection arrangements in place, and marketing and provisioning the local service.

C. The Commission Should Also Declare That The Lock-Up Provisions Contained In ILEC Special Access Tariffs Are Unlawful And Unenforceable.

Historically, the Bells have had a near-absolute monopoly on the provision of last-mile access in their territories. The 1996 Act was intended to inject competition in those markets. First, it sought to eliminate entry and regulatory barriers that prevented the deployment of alternative access facilities where feasible to do so. 47 U.S.C. §§ 251(b), 253. Second, it granted competitive carriers the right to lease the necessary access as “unbundled network elements” at cost-based rates. *Id.* § 251(c)(3).

In either case, these alternatives threatened the Bells’ dominant special access position. Thus, the Bells had two options. Either they could respond to emerging competition by lowering special access rates to reduce the likelihood of bypass. Or they could undertake “exclusionary pricing” strategies that kept traffic on their networks while preserving their ability to charge supracompetitive rates. Predictably, they choose the latter.

The principal vehicle the Bells employed to effectuate this strategy was to enact “overlay” tariffs that require special access subscribers to commit the lion’s share of their total traffic to the Bells for a lengthy term period in return for obtaining the lowest special access rates available. The most vivid example of such a “lock-up” provision is SBC’s Managed Value Plan (“MVP”). Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 55. Subscribers to the MVP obtain significant discounts off of the special access rates that they would otherwise pay under other SBC tariffs. Subscribers to the MVP commit a certain level of traffic. Under the MVP, this minimum commitment level can be increased (but not decreased), and the discounts apply only to the committed revenue, not to any traffic in excess of the commitment. Moreover, the

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MVP subscriber must agree not to use UNEs for more than 5% of its total needs for the functionality provided by special access. But critically, any failure to meet the minimum revenue commitment leads to loss of discounts unless the customer pays SBC the amount of the shortfall. And exceeding the MVP's 5% cap on UNE purchases results in loss of discounts *and* termination, which in turn triggers very severe non cost-based penalties, because the SBC's special access prices are so far above economic cost. *See generally* Stith Dec. At the same time, the subscriber receives no credit for UNE purchases toward the minimum contract requirements.⁶⁴ And notably, the penalties for failing to satisfy these conditions are so severe that they wipe out any gains a subscriber might obtain by purchasing lower cost UNEs or obtaining access from another competitive carrier. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 55. The other Bells' overlay special access tariffs contain similar lock-up provisions that condition the best available rate on agreement by the subscriber to send the lion's share of its traffic to the Bells. *See, e.g.*, BellSouth Tariff FCC No. 1, § 2.4.8; Qwest Tariff FCC No. 1, § 7.1.3(C); Verizon FCC Tariff No. 14, § 5.16.14(A).

The Bells knew that competitors had little choice but to knuckle under to these terms. Because special access competition is nascent and the availability of UNEs is limited, the only way competitive carriers can obtain access to all the customer locations they seek to serve is to use the Bells' special access service. And since these carriers have to purchase special access services and also minimize costs in a competitive market, their only rational choice is to agree to the OPPs' oppressive terms. That is because their only other option is to purchase special access

⁶⁴ By contrast, in competitive markets, discounts are nearly always provided for the full amount of the volumes purchased, even in excess of the minimum commitment level required to earn the discounts. And customers also have the flexibility to place some portion of their business with
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at the much higher prices the Bells charge to carriers that do not agree to lock-up their traffic. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 56. But this is no choice at all. A carrier foregoing the significant discounts available only through the overlay lock-up tariffs is at a significant competitive disadvantage *vis-a-vis* other carriers that obtain the lowest special access rates – and at an enormous disadvantage compared to the Bell itself, which only incurs the significantly lower economic costs of such access. *Id.* The Bells effectively concede this point when they point to the availability of the “discounts” that are only available to carriers that subscribe to the lock-up tariffs as evidence that special access is a substitute for UNEs and make no claim that this is the case for month-to-month special access service. *See, e.g.,* 7/20/04 Verizon Letter at 17.

In contrast, when the Bell long distance affiliates purchase special access from their ILEC affiliates, they are of course more than happy to commit 100% (or more) of their prior volumes in order to maintain the best possible discounts. And even if the Bell affiliate incurs a shortfall penalty, that is merely a left-pocket/right-pocket intra-company transfer that has no real effect.

The lock-up commitments devastate competitive special access purchasers’ ability to shift traffic to alternative suppliers where it is otherwise possible to do so. A carrier that subscribes to a lock-up OPP must agree to provide the vast majority of its traffic to the Bell. That means that even when competitive alternatives exist (possibly even on the carrier’s own facilities), it generally cannot use them without risking the severe penalties triggered by failure to

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other suppliers without economic penalty, thereby providing them some leverage to keep the service provider “honest” by competing for the uncommitted volumes.

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meet the minimum traffic levels the OPPs require.⁶⁵ Indeed, many carriers (but not the Bells' long distance affiliates) are experiencing substantial declines in their retail services, due largely to fierce retail competition coming from the Bells themselves. Thus, the lock-up provisions prevent them from sending any significant amount of incremental traffic over their own facilities, or those of alternative wholesalers. For the same reason, these lock-up provisions prevent those subscribers from shifting significant traffic to UNEs.

The impact of Bells' lock-up terms might be less stark if demand for special access-based services were growing rapidly.⁶⁶ But as explained above, that situation does not apply to competitive carriers today generally, or to AT&T specifically. Because of the Bells' unique customer relationships and cost advantages (derived from their historical position and their ability to obtain access at economic costs), the Bells' long distance affiliates have experienced enormous growth in an extremely short period of time at the expense of established carriers. And the Bells' long distance affiliates obviously have no incentive (let alone ability) to bypass the Bells' own existing facilities. At the same time, the overall market for services that rely on special access is flat (or even contracting in certain segments of the market). Thus, the 90%+ percent lock-up requirements effectively starve alternative suppliers of traffic that would otherwise justify additional facilities expansion.

⁶⁵ The competitive constraints imposed by the lock-up requirement arise when the Bells' access wholesale customers are forced to choose between keeping their service demand on the Bells' networks or diverting it to support their own facilities deployment or purchases from non-Bell suppliers. Where that choice arises, the shortfall liability provisions tied into the lock-up commitment ensure that the Bells – rather than any competitor – will serve the locked-up demand.

⁶⁶ Because the 90%+ purchase commitment is based on historical volumes at the outset of the term, a carrier with growing demand might have increasing amounts of “free” traffic that could be shifted to its own facilities or those of a third party.

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In order to assure that competitive carriers can compete against the Bells by building transmission facilities where it is feasible to do so (and leasing UNEs when they are actually impaired), the Commission should declare in this proceeding that these conditions – which could only have been imposed as a result of the incumbents’ market power – are unlawful and unenforceable. Such action will also ensure that the Bells can keep traffic on their networks only by acting procompetitive, *i.e.*, by lowering prices and raising quality. *See infra* subpart 1. And because carriers have only subscribed to the Bells’ OPPs because of anticompetitive limitations on access to UNEs over the past eight years and the lack of competitive alternatives, the Commission should provide competitive carriers with a “fresh look” so that they can now purchase UNEs where they are lawfully entitled to do so. *See infra* subpart 2.

1. The Bells’ Lock-Up Provisions Violate The Communications Act And Directly Undermine The Commission’s Local Competition Policies.

There are several related reasons why the Bells’ lock-up requirements contained in their OPP “overlay” tariffs violate the Communications Act and the Commission’s policies designed to foster local competition. Therefore, the Commission should use this proceeding to put an end to these practices, for three separate reasons. First, the lock-up provisions severely inhibit the potential for additional facilities-based competition. Second, those provisions are directly inconsistent with the Commission’s policy to sustain and support special access competition. And third, the provisions are unjust, unreasonable and discriminatory in violation of § 201(b) and § 202(a).

First, the Bell lock-up provisions are unlawful because they impede nascent facilities-based competition, particularly in markets for the provision of special access services, and thus undermine Commission policies designed to foster such competition. A tariff provision that undermines competition and related Commission policies is unreasonable and thus unlawful

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under Section 201(b) (and, often, Section 202(a)). *See Volume Discount Order* ¶¶ 12, 14; *Tariff 15 Order* ¶ 23; *Pricing Flexibility Order* ¶ 163.

The Act and Commission policies seek to foster competition, particularly facilities-based competition, in special access and related markets. Congress intended the 1996 Telecommunications Act “to provide for a pro-competitive, de-regulatory national policy framework designed to accelerate rapidly private sector deployment of advanced telecommunications and information technologies and services to all Americans by opening all telecommunications markets to competition.” S. Rep. No. 104-230, at 1 (1995). To this end, the Act is designed to facilitate competition, both through the resale of particular elements and services of the monopoly local exchange networks and by ensuring that neither monopolists nor state regulators improperly restrict competitive entry, including facilities-based entry. *See AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 371 (1999); *see also* S. Rep. No. 104-230, at 1. Development of facilities-based competition is an especially important objective of the Commission’s policies and its implementation of the Act. *See Triennial Review Order* ¶¶ 22, 70, 114, 200, 242, 448; *Local Competition Order* ¶¶ 172, 325, 635, 685. Indeed, the Commission expressly relied upon the development of facilities-based special access competition as the very basis for granting the Bells broad special access pricing flexibility. *See Pricing Flexibility Order* ¶ 141.

But the lock-up commitments seriously undermine these goals. The Commission has correctly found that a competitor’s ability to secure sufficient traffic on a particular route is a prerequisite to its deployment of the transmission facilities necessary to support facilities-based competition. A competitive carrier’s decision to build transmission facilities is made on a route-by-route basis, and is a function of how much traffic that competitor can serve on that route, both

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for its own retail customers and on a wholesale basis for other carriers. As explained in Part II *supra*, a carrier that plans to construct transmission facilities must incur enormous upfront fixed costs for structures, trenching, poles and conduits, and rights of way before it can provide service. These fixed costs do not vary significantly with the size or capacity of the fiber deployed. *Triennial Review Order* ¶ 206 (“For fiber-based loops, the cost of construction does not vary significantly by loop capacity, *i.e.*, the per-mile cost of building a DS1 loop does not differ significantly from the cost to construct an OCn loop. The most significant portion of the costs incurred result from deploying the physical fiber infrastructure in the ground, rather than from lighting the fiber optic cable.”), *id.* ¶ 386 (“the cost of deploying a transmission facility does not vary significantly with capacity because much of the cost of the facility is related to the deployment itself, such as trenching or attaching to poles, rather than the cost of cabling and other equipment”); *see also id.* ¶¶ 303, 371. The costs are also largely sunk. *Id.* ¶ 203, 237, 303, 360.

In light of these constraints, facilities-based entry is impossible unless a competitor has established a viable customer base before it begins any new construction or makes any substantial new investment. New entrants that have little or no traffic on a given route obviously lack any economic justification to construct facilities on that route, because they simply cannot expect enough revenue to offset the enormous fixed and sunk costs of deployment. Thus, the Commission properly found that “competitive carriers with lower amounts of traffic aggregation, such as new market entrants, face economies of scale that can act as a barrier to entry.” *Id.* ¶ 377 & n.1155; *see also id.* ¶ 303 & n.890. And because those costs are sunk, a competitor must have assurance that it can continue to carry sufficient traffic (and earn sufficient revenues) over the economic life of the facilities. *Id.* ¶ 88. Given these real world requirements, a carrier cannot

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justify constructing facilities unless it has *already* accumulated sufficient commitments for traffic on a route to cover the up-front and sunk costs of construction. D’Apolito-Stanley Dec. ¶¶ 6-8. Competitive carriers that did not adhere to this principle in the 1990s and operated on a “build it and they will come” principle have largely disappeared from the landscape, or forced their investors through at least one bankruptcy reorganization. Selwyn Dec. ¶¶ 21, 30-31.

The Bells’ overlay OPPs are clearly designed to – and have the effect of – starving competitive carriers of the traffic they need to deploy and maintain bypass facilities. The lock-up requirements’ constraints on special access competition have a significant impact at the exact moment when a competitive alternative may otherwise be a viable option. The impact is most acutely felt when a Bell special access customer has a choice between keeping its service demands on the Bell’s network or diverting it to support its own facilities deployment or to purchase a wholesale alternative from a Bell competitor. Where such a choice arises, the shortfall liability provisions that are paired with the Bells’ 90%+ commitment ensure that the Bell – not its competitors – will carry the locked-up demand, as well as a substantial “buffer” above the commitment level that any prudent carrier would maintain. And as the Bells’ aggressive long distance entry diminishes the market share of the established carriers that are the biggest OPP subscribers, less and less traffic will be available either for competitive wholesalers or new self-deployed facilities.

For the same reasons, the Bells’ OPPs inhibit special access subscribers from converting to UNEs, in direct contravention to the Commission’s findings that competitive carriers should be able to use these facilities to provide telecommunications services where “impairment” exists. Indeed, in the case of SBC’s MVP tariff, there is an independent restriction that limits the extent to which a subscriber can purchase UNEs, even if it has “head room” under the OPP.

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Second, because the Bell lock-up provisions are structured on a region-wide and service-wide basis, they directly thwart and contradict the Commission's policies designed to foster special access competition on the one hand and provide appropriately tailored regulatory relief to the Bells on the other. The Bells' OPPs leverage their market power in areas and for services in which competition indisputably does not exist in order to prevent competition in areas and services for which it could potentially develop.

Monopolists' ability to undertake such exclusionary pricing strategies has been well documented in the economics literature.⁶⁷ As this literature explains, a dominant monopolist can adopt pricing strategies that prevent competition when customers cannot shift all of their demand to rivals. The monopolist can do so by conditioning its pricing for the monopoly portion of the customer's demand on the customer's choices for the competitively sensitive portion of the demand. In this way, the dominant firm can leverage its monopoly over the customer's "base" demand – where the customer has no viable option – to raise the customer's costs substantially. Such exclusionary pricing is effective precisely because it forces a customer to pay a higher price

⁶⁷ See Phillippe Aghion and Patrick Bolton *Contracts as Barriers to Entry*, American Econ. Rev. 388-401 (June 1987); Eric Rasmusen, J. Mark Ramseyer, and John Wiley, *Naked Exclusion*, American Econ. Rev. 1137-45 (Dec. 1991); Illya Segal and Michael Whinston, *Naked Exclusion: Comment*, American Econ. Rev. 296-309 (March 2000); see also W. Tom, D. Balto, and N. Averitt, *Anticompetitive Aspects of Market-Share Discounts and Other Incentives to Exclusive Dealing*, 67 *Antitrust L.J.* 615, 615 (2000) (“(1) market-share discounts structured to produce total or partial exclusivity should be judged according to the same economic principles that govern exclusive dealing; and (2) the case law, properly construed, permits such discounts to be condemned under the Sherman Act or FTC Act if they produce anticompetitive effects without counterbalancing procompetitive effects.”).

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on its demand in monopoly areas if it deals with a competitor for its competitively sensitive demand.⁶⁸

The Bells' OPPs are a textbook example of such exclusionary pricing. The pricing for OPPs is generally structured on a "region-wide" and "service-wide" basis. That is, the minimum usage commitment is determined on the basis of a customer's *overall* traffic in the *overall* region served by the RBOC and for a broad range of access services (DS1, DS3, OCn). Thus, customers do not have the option of satisfying the lock-up in particular discrete geographic areas (*e.g.*, a particular city) or for a particular class of facilities (*e.g.*, OCn-level access). As a result, they must lock-up their traffic *both* in locations *and* for services for which alternatives may exist, as well as for those where they do not.

The Bells' lock-up provisions thus have a devastating impact on competition. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶¶ 8-60. Where a carrier must obtain access throughout a Bell's territory, the OPPs ensure that it cannot choose to deal with a competitor for the locations and services where alternatives exist and the Bell in the instances where they do not. Instead, the only way a competitor can obtain access in the monopoly markets where there is indisputably *no* alternatives is to also agree to lock-up traffic in those areas where bypass is potentially available. For example, carriers typically have no choice but the Bells for DS1 level access. But a competitor cannot satisfy the requirements of the lock-up provisions if it wishes to

⁶⁸ The Department of Justice has recognized this point as well. *See United States v. Microsoft*, 59 Fed. Reg. 42,845, 42,854 (Aug. 19, 1994) (Competitive Impact Statement) ("While the Department recognizes that volume discount pricing can be and normally is pro-competitive, volume discounts can also be structured by a seller with market power (such as Microsoft) in such a way that buyers, who must purchase some substantial quantity from the monopolist, effectively *are coerced by the structure of the discount schedule* (as opposed to the level of the price) to buy all or substantially all of the supplies they need from the monopolist.") (emphasis added).

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purchase only DS1 services from the Bells, which would allow it to buy higher level access services (for which alternatives may exist) from competitors. Instead, under the Bells' overlay tariff structure, the competitor can only obtain the discount on DS1 services if it *also* foregoes competitive alternatives (or self-deployment of its own facilities where it would be economic to do so) on other services. Likewise, a carrier cannot purchase access from competitive carriers in dense urban areas (where there may be some competition) and obtain a discount from the Bell on the access it needs to compete in more suburban and rural areas where there is no competition. In each instance, the region- and service-wide requirements imposed by the OPP require the subscriber to use the Bell for the vast majority (if not all) of its access needs.

This aspect of the Bells' OPPs is directly contrary to the purpose of the *Pricing Flexibility Order*. It enables the Bells to foreclose competition in pricing flexibility MSAs by leveraging their undisputed monopoly power in non-pricing flexibility MSAs. Thus, even if the Commission's pricing flexibility triggers accurately measured whether new entry could constrain Bell pricing power (and they clearly do not), the Bells' OPPs ensure that new entrants cannot obtain the traffic necessary to fund facilities deployment.

Critically, this foreclosure exists even if alternative suppliers offer highly advantageous rates. The shortfall penalties in the OPPs are so severe that even if a alternative supplier offers a rate that is discounted far bellow the Bell's best price, it would still not be economically sensible for the competitive carrier to purchase that alternative, because it may trigger the OPP shortfall provision. Benway-Holleron-King-Lesher-Mullan-Swift Dec. ¶ 58. The result, of course, is to choke off the flow of traffic that might be available to competitive carriers in pricing flexibility markets – markets where the Commission is relying on the presence of such competitors to constrain the Bells' enormous market power.

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The Bells' OPPs are analogous to practices that are routinely condemned under the antitrust laws. In practice, the OPPs are tying arrangements that "deny competitors free access to the market for the tied product, not because the party imposing the tying requirement has a better product or lower price but because of his power or leverage in another market. At the same time buyers are forced to forego their free choice between competing products." *Northern Pac. Ry. v. United States*, 356 U.S. 1, 6 (1958). Moreover, this type of tying arrangement is "regarded as inherently anticompetitive and a *per se* antitrust violation because it shields an inferior product from competition, excludes legitimate competitors from the market, forecloses the buying public's ability to choose products on a merit basis, and reduces competition which would otherwise bring lower prices and better quality to the marketplace." *Amerinet, Inc. v. Xerox Corp.*, 972 F.2d 1483 (8th Cir. 1992) (citing *Jefferson Parish Hospital Dist. No. 2 v. Hyde*, 466 U.S. 2, 12-15 (1984)).

The OPPs are also analogous to unlawful requirements contracts. A contract that effectively requires customers to purchase most or all of their requirements for a product or service from a monopolist is often found to be anticompetitive when a significant portion of the market (generally in excess of 30-40 percent) is affected or "locked up" by the contract. *See, e.g., Tampa Elec. Co. v. Nashville Coal Co.*, 365 U.S. 320 (1961); *Jefferson Parish*, 466 U.S. at 45 (Brennan, J., concurring); *see also See United States v. Microsoft Corp.*, 253 F.3d 34, 70(D.C. Cir. 2001) (referencing the "40% standard drawn from the caselaw"); *Twin City Sportservice, Inc. v. Charles O. Finley & Co.*, 676 F.2d 1291 (9th Cir.), *cert. denied*, 459 U.S. 1009 (1982) (24 percent combined with long term contracts). Professor Hovenkamp suggests twenty per cent (20 percent) as an appropriate minimum foreclosure percentage. *See XI Antitrust Law* ¶ 1821c at 164 (*prima facie* case would require a showing of at least 20% or more foreclosure in the

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downstream market and a concentrated upstream market with at least 1800 HHI and defendant has at least 20% market share; other factors to be considered for *prima facie* case include the presence of barriers to entry; *id.* ¶ 1821 at 151 and ¶ 1821d at 165-170). Here, these elements are far exceeded. The foreclosure far exceeds 20 percent; high barriers to entry exist; and the Bells' provision of special access far exceeds 5,000 HHI under even the most generous assumptions regarding market share.

Finally, and equally important, the Bells' monopoly power over special access facilities in all of their areas is demonstrated by the fact that the Bells can and do charge higher prices for special access than alternative suppliers do. *See Microsoft*, 253 F.3d at 51. The Supreme Court defines monopoly power as "the power to control prices or exclude competition." *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377 (1956). More precisely, a firm is a monopolist if it can profitably raise prices substantially above the competitive level. 2A Phillip E. Areeda *et al.*, Antitrust Law ¶ 501, at 85 (1995); *cf. Ball Mem'l Hosp.*, 784 F.2d at 1335 (defining market power as "the ability to cut back the market's total output and so raise price"). Where evidence indicates that a firm has in fact profitably done so, the existence of monopoly power is clear. *See Rebel Oil Co. v. Atl. Richfield Co.*, 51 F.3d 1421, 1434 (9th Cir.1995); *FTC v. Indiana Fed'n of Dentists*, 476 U.S. 447, 460-61 (1986) (using direct proof to show market power in Sherman Act § 1 unreasonable restraint of trade action).

Here, the anticompetitive effect is particularly pronounced, because the "contract" is a take-it-or-leave-it tariff crafted by the monopolist and because a very significant portion of the relevant market is affected by these arrangements for a lengthy period. In light of AT&T's share of the large business market, which is heavily dependent on functionality provided through special access services, AT&T's forced commitments under the Bells' OPPs alone may well

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satisfy the antitrust standard, especially since the Bells' long distance affiliates must also effectively lock up their demand as well.

In short, through the sheer power generated by its market position in “non-competitive” markets, the Bells have forced customers that want to purchase special access at discounted rates in markets and for services where the competitors have no alternatives also to purchase special access from the Bells in markets and for services where they may (although rarely in practice, do) have some alternatives. The Bells are thus leveraging their undisputed (and indisputable) market power to foreclose competition in areas where it might otherwise develop.

Third, carriers with identical traffic volumes are charged different rates under the Bells' OPPs; thus, they are unjust, unreasonable and discriminatory in violation of § 201(b) and § 202(a). Absent this discrimination, the Bells would be forced to respond with steeper discounts to carriers with the highest traffic volumes that have the greatest potential to self-deploy their own facilities or provide “seed” traffic to alternative providers.

For two decades, extending back to the 1984 *Volume Discount Order*, the Commission has issued clear guidance as to the difference between legitimate and unlawful discount plans.⁶⁹ Those precedents establish that permissible discounts may reflect only “efficiently-priced volume discounted offerings” of “reduced per-unit prices for a particular number of units of service.” *Volume Discount Order* ¶¶ 43-44. In so ruling, the Commission has expressly sought “to eliminate the carrier’s ability to discriminate by targeting a volume discount to a particular segment of customers through restrictions.” *Id.* ¶ 41. Thus, “incumbent LECs must make

⁶⁹ See *Volume Discount Order* ¶¶ 43; *Access Reform Order* ¶ 187; *Pricing Flexibility Order* ¶ 126; *Tariff 12 Order* ¶ 69; *Tariff 15 Order* ¶ 16; *Third Transport Rate Order* ¶ 114; *Fourth Transport Rate Order* ¶ 17.

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[volume discounts] available to any customer with sufficient volumes,” *Pricing Flexibility Order* ¶ 124, and may not have customers “who order the same quantity of a service with volume discounts charged different rates,” *Volume Discount Order* ¶ 38.

The Bells’ lock-up provisions flout these precedents. A customer with a specific level of demand that is willing to deal (almost) exclusively with the Bell receives a special discount, but a customer that is willing to commit the *exact same level of demand* in the future (but wishes to divert a portion of its demand to a Bell competitor) is barred from receiving the discount. At the same time, there is clearly no difference in the cost in serving these two customers, as both have committed the same level of demand. Such difference in treatment is the *sine qua non* of unreasonable discrimination. As pointed out by Nobel Laureate George Stigler, price discrimination occurs when a good or service of a particular cost is sold at differing prices to different consumer groups. George J. Stigler, *Theory of Price* 209 (1966).⁷⁰

The Bells’ lock-up provisions stand in stark contrast to legitimate cost-based volume discounts. The latter recognize efficiencies and lower costs “associated with larger volumes of traffic.” *Expanded Interconnection Order* ¶ 199; see also *Volume Discount Order* ¶¶ 34-36. In contrast, the Bells’ lock-up provisions offer discounts to customers (such as the Bells’ long distance affiliates) with small volumes that are willing to commit that they will not deal with the Bells’ competitors for the lion’s share of their prior demand, and deny those same discounts to customers (such as the Bells’ long distance competitors) with far *greater* volumes that wish to

⁷⁰ This discrimination is also conclusive evidence that the Bells have market power over special access services. It is well established that such discrimination only arises as a consequence of embedded market power. See Jean Tirole, *The Theory of Industrial Organization*, 133-168 (1989); David Kaserman & John Mayo, *Government and Business: The Economics of Antitrust and Regulation*, 271-296 (1995).

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deal with the Bells' competitors (or use their own facilities) for a material portion of their demand. The lock-up provisions thus enable the Bells to limit the availability of volume discounts in precisely the manner that the Commission has prohibited. *See Volume Discount Order* ¶¶ 38, 41; *Pricing Flexibility Order* ¶ 125.

The lock-up provisions are also unreasonable and discriminatory in violation of § 201(b) and § 202(a) for another reason. These provisions require a carrier to commit to send the Bell a certain percentage of its demand that is based on the carrier's historical usage. But that means that carriers facing declining demand may simply be unable to meet a volume commitment threshold even if they would be willing to lock-up *all* of their traffic to the Bell. Because the Bells' commitment floors are so high (requiring that customers maintain 90% to 95% of their historical demand for a multi-year period), there is a serious risk that a carrier with declining demand may be pushed into shortfall and face potentially significant penalties that outweigh any benefit that it would gain from temporarily getting the discounted rates.

This is not a mere theoretical risk in today's market conditions. The Bells' increasing long distance market shares for business customers has, of course, come at the expense of established carriers. *See supra* Part III.C.2. And as established carriers lose business to the Bells, they in turn have lower quantities of special access traffic that can be used to satisfy the lock-up requirements.

This again shows that the Bells' lock-up tariffs are unreasonable and discriminatory. Under the OPPs, the price that a carrier pays depends *not* on how much it costs to provide the service, but the extent to which the carrier's retail services have increasing or decreasing demand. Again, this has the clear effect of benefiting the Bells' long distance affiliates and hurting the Bells' competitors.

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Finally, the Bells' special access plans lock up significant amounts of supply for an unreasonable length of time, usually for periods of three to five years at a time. Competition law analysis examines these types of plans to ensure that their duration does not preclude competitive opportunities. A three or five-year plan would be deemed an unreasonable restriction on competition when employed by a firm with market power. *See FTC v. Motion Picture Advertising Serv. Co.*, 344 U.S. 392, 395-96 (1953). In *Motion Picture*, the exclusive dealing arrangements in question were the agreements between distributors of films that advertised products for sales and theatre owners. Under the agreement, the theatre owner was to show only advertising films from a single distributor. In this case, four distributors had exclusive dealing contracts with 75% of the theatres in the United States. The exclusive dealing arrangements lasted up to five years. *Id.* at 393-94.

2. The Commission Should Enjoin Enforcement Of Tariff Provisions That Give Effect To The ILECs' Unlawful Lock-Up Provisions.

Not only should the Commission declare that the lock-up provisions of OPP are unlawful, it should also eliminate the liability provisions that lend to their anticompetitive effect. In *Triennial Review Order*, the Commission held that it had ample authority to eliminate even the termination liability provisions of the OPPs and grant subscribers a fresh look. *Triennial Review Order* ¶ 698. However, the Commission declined to grant competitive carriers an across-the-board fresh look with respect to the full range of the Bells' term special access arrangements on the grounds that there was not sufficient evidence to show that these deals were the reflection of Bell "market power," and that "abrogation of negotiated terms" that "link[ed] a price discount to a contractual term" would not be justified on a comprehensive basis (but could be satisfied in individual proceedings). *Id.* In particular, the Commission observed that it was quite common in

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a variety of settings to see contracts that gave discounts on the basis of term and volume commitments. *Id.*

The “market power” evidence that the *Triennial Review Order* found lacking is clearly before the Commission now. Carriers have purchased Bell special access services *only* because they had no other alternative. As explained in Part II, competitive deployment of DS_n-level facilities at the line limits imposed in the *Triennial Review Order* is not economic and these facilities are at best only rarely available from third parties.

In addition, the overlay discount plans are very different from the contractual arrangements and the vast majority of the OPPs that the Commission previously addressed. Most ILEC discount arrangements, including most OPPs, allow the customer to select the amount of demand that will be subject to the term commitment. The plans discussed above, in contrast, have an especially anticompetitive effect because they require a customer to continue to commit to the ILEC all or nearly all of its previous special access purchases. That is, through a generally available tariff (not a contract, or even a contract tariff), the ILEC sets the percentage of prior demand for which the customer must refuse to deal with the ILEC’s competitors and presents an all-or-nothing offer. These are not the “long term special access contracts” or “negotiated terms” that the Commission previously reviewed.

Likewise, carriers were not able to avoid the need to buy special access by purchasing UNEs. A series of Commission rulings arbitrarily and unlawfully denied competitive carriers access to UNEs during the time when they agreed to purchase special access under the OPPs. Foremost, the Commission’s use restrictions prohibited IXC’s such as AT&T from purchasing UNEs to provide long distance services even in instances where they could not self-deploy their own facilities or obtain them from third parties. Indeed, as the Commission itself has

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recognized, the specific criteria it had initially promulgated to implement its use restriction policy were overinclusive and often denied competitive carriers access to EELs even when they were seeking to use those EELs to provide *local* services. *Triennial Review Order* ¶¶ 612-19. Relatedly, the Commission’s now (properly) abandoned “co-mingling” rule prohibited competitive carriers from connecting UNEs to provide even local services where they also were purchasing tariffed services. *Triennial Review Order* ¶¶ 579, 581; *see also Ex Parte* Letter from Andrew Lipman, Cbeyond *et al.*, to Marlene Dortch, at 2 (filed in CC Docket 01-338, Aug. 8, 2004) (“8/9/04 Swidler Letter”).

Competitive carriers were also unable to purchase UNEs for a considerable period – and thus were remitted to special access services – because the Eighth Circuit twice struck down (incorrectly) the Commission’s rules requiring loop-transport combinations. It was not until the Supreme Court’s *Verizon* decision in 2002 that it was finally settled that competitive carriers were permitted to obtain existing and new UNE combinations.

Finally, the Bells have engaged in self-help to thwart access to UNEs. The Bells’ refused to provide UNEs to competitive carriers where they claimed that the request required even a routine “modification” of their network. *Triennial Review Order* ¶¶ 632-41 (finding the Bells “no facilities” practice unlawful). Remarkably, the Bells continue to deny competitive carriers UNEs today on this basis. 8/9/04 Swidler Letter at 2. And, as just explained, the Bells’ “lock-up” tariffs have forced competitive carriers to maintain traffic on special access tariffs when they would otherwise have purchased UNEs. Indeed, SBC’s MVP tariff expressly limits the extent to which a competitive carrier can purchase UNEs and still obtain special access discounts.

Competitive carriers thus did not agree to the terms of the Bells’ OPPs as the result of any arm’s length “commercial negotiation,” but rather because they had *no other choice* in order

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to obtain the access that they needed to serve customers. Moreover, the Bells' OPPs are not simple term/volume deals. *Cf. Triennial Review Order* ¶ 698. As shown above, they impose an additional condition upon subscribers: they must agree to lock-up the vast majority of their traffic with the Bell and not deal with the Bells' rivals. For this reason, the prices the Bells charge for special access are not legitimately related to a carrier's traffic volume, but turn fundamentally on the non-cost aspects of the pricing plan: the purchaser's agreement to lock-up whatever amount of traffic it has with the Bell. This type of patent price discrimination would be simply impossible in a competitive market.

Under these circumstances, enjoining enforcement of liability provisions is warranted. In concept, this is even less intrusive than the Commission's prior decision to allow customers to terminate Tariff 12 services without termination liabilities when 800 numbers became portable. *See e.g., Interexchange Competition Order*, 8 FCC Rcd 2659 (1993). The Commission granted that fresh look because when customers signed contracts with AT&T for 800 service they largely had no alternatives. Simply allowing 800 number portability would not have induced competition if customers were also not freed from their term contracts. So too here, competitors will be hamstrung if they incur liability because they do not meet the take-it-or-leave-it commitment requirements that are clearly unlawful.

Finally, the term liability provisions are not "appropriate" penalties. *UNE Remand Order* ¶ 486 n.985 (emphasis added). The Commission has no discretion to allow unlawful tariff terms to remain in effect, and allowing the Bells to assess liabilities would serve only to guarantee continuation of the Bells' monopoly profits and thus would clearly not be "appropriate." By definition, UNEs priced at TELRIC recover the carrier's costs and are fully compensatory. *See generally Verizon Communications, Inc. v. FCC*, 535 U.S. 467 (2002). Requesting carriers are

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legally entitled to purchase unbundled network elements when they are impaired without them, and Bells cannot lawfully impose termination liabilities on competitive carriers that are designed solely to recoup monopoly profits in excess of TELRIC as the price of exercising those rights. *See* 47 U.S.C. § 252(d)(1).

V. THE COMMISSION SHOULD REAFFIRM ITS REQUIREMENT THAT ILECS IMPLEMENT SEAMLESS AND COST-EFFECTIVE BATCH CUT PROCESSES.

The establishment of an effective, efficient batch cut migration process – “a seamless, low-cost process for transferring large volumes of customers” (*Triennial Review Order* ¶ 423; *see also id.* ¶ 487) – is an essential component of any transition from the UNE-P to the provision of service through the competitive carriers’ own facilities. As the Commission correctly found in the *Triennial Review Order*, the ILECs’ processes for migrating individual “hot cuts” erect both operational and economic barriers that hinder facilities-based competition, and sometimes prevent it entirely. *E.g., id.* ¶¶ 459, 464-473.

The *Triennial Review Order* recognized that the hot cut process “could be improved if cut overs were done on a bulk basis, such that the timing and volumes of the cut over is better managed.” *Id.* ¶ 474. Of course, a batch cut process can only “mitigate” the operational and economic barriers of the basic hot cut process. *Id.* ¶¶ 423, 475, 487. A batch cut process will still include the same manual cutover work and certain other inefficiencies of the basic hot cut process that the *Triennial Review Order* found to be serious problems for both competitive carriers and their end-users. *Szczepanski-Van de Water-Norris Dec.* ¶¶ 25-27, 32.

Nonetheless, a properly designed and implemented batch cut process can enable a competitive carrier to realize efficiencies and cost savings that are unavailable under the basic hot cut process. *Id.* ¶ 33. For example, by allowing competitive carriers to order hot cuts at one time in a “batch,” a batch cut process can enable a competitive carrier to use its resources more

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efficiently in tracking hot cut orders, performing pre-cutover and post-cutover testing, activating the number port, and performing a variety of other activities related to the cutover process. *Id.* ¶¶ 33, 35-37. A batch cut process also can give a competitive carrier more flexibility in scheduling the time of the cut to meet the needs of its customers. *Id.* ¶ 34. AT&T's own experience in using a project managed process in its "UNE-P strategy" confirmed the potential of the batch cut process for achieving quality and efficiency gains. *Id.* ¶¶ 33, 46-52.

It was precisely because of these potential gains that the *Triennial Review Order* concluded that an efficient, lower-cost batch cut process was "necessary, at a minimum, for carriers to compete effectively in the mass market."⁷¹ The *Triennial Review Order* went even further, expressly requiring state commissions to approve and implement, within nine months, a batch cut process that "will render the hot cut process more efficient and reduce per-line hot cut costs." *Triennial Review Order* ¶ 460.

That, however, has not happened. Although states began to actively address batch hot cut processes as part of the review originally required by the *Triennial Review Order*, only a few of those proceedings have come close to meeting the expectations of the Commission's directive. Instead, nearly fourteen months after the issuance of the *Triennial Review Order*, and in the wake of *USTA II*, most state commissions have either suspended their proceedings or closed them altogether. *See* Szczepanski-Van de Water-Norris Dec. ¶¶ 30, 204 & Att. 1 (describing status of state proceedings involving batch hot cuts).

⁷¹ *Triennial Review Order* ¶ 487. *See also, e.g., id.* ¶ 474 (batch cut process is "likely to be essential to overcome the operational impairment that competitors face in serving mass market customers").

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For their part, the ILECs have proposed batch cut processes that are plainly inconsistent with the requirements that this Commission identified as essential in the *Triennial Review Order*. The ILECs’ processes have not even been comprehensively tested to determine whether they work as promised – much less whether they are seamless and efficient. *Id.* ¶¶ 94-109. But even on paper, those processes are woefully deficient. *E.g., id.* ¶¶ 59-70, 75-83, 121-138, 160-64. To add insult to injury, in many states the ILECs have proposed rates for their batch cut processes that are even higher than those the *Triennial Review Order* found to be unreasonable in the context of the basic hot cut process. *Id.* ¶¶ 176-188.

The need for a seamless and low-cost batch cut process, however, is as critical today as it was when the *Triennial Review Order* was issued. *Id.* ¶¶ 32-37. In view of the inactivity of most state commissions, and the ILECs’ failure to implement adequate processes, the Commission must take decisive action if the batch cut processes it envisioned – and facilities-based competition – are ever to become a reality. Without Commission action to set baseline requirements, leaving the issue for the state commissions to resolve will all but ensure that the operational and economic barriers erected by the hot cut process will continue. As the *Triennial Review Order* found, absent the establishment of a an effective batch cut process, competitive carriers “are likely to be unable to economically serve a market characterized by low margins.” *Id.* ¶ 474.

Thus, it is not enough that the Commission reaffirm its overall commitment to a seamless, lower-cost batch cut process, or once again require that State commissions take action. The Commission should – indeed, must – establish requirements and standards to maximize the effectiveness of batch cut processes for competitive carriers. First, the Commission should make clear that a batch cut process must include *all* migrations of loops from one carrier’s switch to

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another, regardless of the type of loop involved and regardless of the identity of the carrier to whose switch the loop is being migrated. Sczepanski-Van de Water-Norris Dec. ¶¶ 53-83. ILECs therefore should not be permitted to exclude from their processes: (1) loops served by Integrated Digital Loop Carrier (“IDLC”) and (2) migrations of loops to the switch of a third party. *Id.* Restrictions on IDLC-served loops of the type adopted by Verizon, BellSouth, and Qwest effectively preclude competitive carriers from using the batch cut process for a significant number of lines. *Id.* ¶¶ 55-73. Similarly, BellSouth’s exclusion of migrations to third-party switches from its batch cut process impairs the ability of competitive carriers such as AT&T to use such switches to serve a significant number of customers when, as is often the case, constructing the necessary collocated facilities would be prohibitively expensive. *Id.* ¶¶ 12, 74-83.⁷²

Second, the Commission should establish requirements to ensure that batch cut processes are economical and efficient for competitive carriers. Most importantly, the Commission should require that any ILEC’s proposed batch cut process be comprehensively tested by a third party, under certain specified testing criteria, before the ILEC may make it commercially available to competitive carriers. *Id.* ¶¶ 87-93.⁷³ The Commission should also require that CLECs are given

⁷² Some of the ILECs have included these types of migrations in their processes, *without* imposing such restrictions. *See* Sczepanski-Van de Water-Norris Dec. ¶¶ 69-70 (SBC includes IDLC-served loops in its batch migration process); *id.* ¶ 83 (Verizon, SBC, and Qwest do not exclude cutovers of loops to another party’s switch from their batch cut processes). There is no reason why all ILECs cannot do the same.

⁷³ *See* Sczepanski-Van de Water-Norris Dec. ¶¶ 111-114 (describing the testing criteria that the Commission should adopt). As part of these standards, the Commission should mandate the two-stage testing proposed by the competitive carriers in the current collaborative proceeding before the Michigan Public Service Commission. The first stage of the test would evaluate the process using pseudo-customer or test lines. The second stage – which would commence only after the first stage had been deemed complete and successful – would utilize the process to migrate
(continued . . .)

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sufficient control over (inter alia) the timing and sequence of the batch hot cuts in order that the cutover will occur at the time least inconvenient to the end-user. *Id.* ¶¶ 115-138. Finally, the Commission should require that the ILEC’s operational support systems associated with the batch cut process (1) provide the status information and functionalities that a competitive carrier needs to effectively monitor, track, and verify batch cut orders and to take any necessary corrective action upon any issues arising from the requested cutovers throughout the entire hot cut process; and (2) maximize the flow-through capability of batch cut orders. *Id.* ¶¶ 147-172.⁷⁴

Third, the Commission should reaffirm the requirement of the *Triennial Review Order* that the ILECs’ non-recurring charges for batch hot cuts must be consistent with TELRIC methodology. *See Triennial Review Order* ¶ 489 (“if they have not done so already, state commissions should adopt TELRIC rates for the batch cut activities they approve”). As the Commission recognized, excessive NRCs, combined with the significant internal costs that a competitive carrier must incur in connection with hot cuts, would make it “prohibitively expensive” for a competitive carrier to use its own facilities. *Id.* ¶ 470. The ILECs’ proposed or actual NRCs for their batch cut processes, however, would achieve precisely that result. As previously indicated, in many states the ILECs’ NRCs exceed the levels that the Commission found to be too high for hot cuts. *Szczepanski-Van de Water-Norris Dec.* ¶¶ 176-188. Some of

(. . . continued)

actual customers of the competitive carriers. In both stages, any problems that were detected would be fixed as they occurred, with subsequent testing to ensure that the “fix” worked. *Id.* ¶¶ 112-113 and Att. 6.

⁷⁴ Although still inadequate in some respects, Verizon’s “WPTS” system is the only notification tool offered by ILECs that generally provides most of the information and functionalities a competitive carrier needs to monitor, track, verify, and take corrective action on hot cut orders. *Szczepanski-Van de Water-Norris Dec.* ¶¶ 151-59. None of the ILECs’ OSS provide sufficient flow-through capability for UNE-L orders. *Id.* ¶¶ 160-164.

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these NRCs, in fact, exceed the ILECs' current rates for individual hot cuts, despite the Commission's expectation that the batch cut process would be "low-cost" and would "result in some *reduction* of the non-recurring costs" of the hot cut process. *E.g., id.* ¶ 182.⁷⁵

Finally, the Commission should adopt performance measurements and standards specific to the batch hot cut process, and require the inclusion of these metrics in the ILECs' existing performance incentive plans (penalty plans). Sczepanski-Van de Water-Norris Dec. ¶¶ 192-203.⁷⁶ Absent such action, the ILECs will have no incentive to make their batch cut processes work seamlessly and efficiently. *Id.* ¶ 192.⁷⁷ No such metrics are currently in place, and state commissions have not acted to establish them. *Id.* ¶¶ 196-97.⁷⁸ In addition, the Commission

⁷⁵ See *Triennial Review Order* ¶¶ 423, 474, 487 (emphasis added). See also, *e.g., id.* ¶ 460 (State commissions must implement a batch cut process that will "reduce per-line hot cut costs"); *id.* ¶ 489 (rates for batch hot cuts "should reflect the efficiencies associated with batched migrations of loops to a competitive LEC's switch, either through a reduced per-line rate or through volume discounts"); 47 C.F.R. § 319(d)(2)(ii)(A)(4) (same).

⁷⁶ These metrics include, for example, the flow-through rate for batch cut orders; average offered interval; average provisioning interval; percentage of batch hot cuts started on time; percentage of batch hot cuts completed on time; percent of trouble reports; and average duration of any service interruption. Sczepanski-Van de Water-Norris Dec. ¶ 199. The *Triennial Review Order* specifically cited some of these metrics as evidence that state commissions should consider in determining whether "the hot cut process imposes an operational barrier." *Triennial Review Order* ¶ 512 n.1574.

⁷⁷ The *Triennial Review Order* recognized the need for such metrics, standards, and penalties. See, *e.g., Triennial Review Order* ¶ 474 (finding ILECs' Frame Due Time and project managed approaches to be inadequate because "there generally are no performance intervals associated with these approaches" and the ILECs therefore "are not subject to financial penalties for inadequate performance"); *id.* ¶ 489 (authorizing state commissions to require ILECs to comply with completion interval metric and other metrics "for provisioning high volumes of loops"); *id.* ¶ 512 n.1574 (describing types of performance data that state commissions should consider in determining whether ILEC is able "to transfer loops in a timely and reliable manner").

⁷⁸ In fact, the ILECs have argued that such metrics and penalties can simply be established *after* they implement their batch cut processes. Such an approach is totally unacceptable, because it would preclude competitive carriers and regulators from determining whether the process is performing adequately. Sczepanski-Van de Water-Norris Dec. ¶¶ 197-98.

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should require that, to the maximum extent possible, the benchmarks or standards for these metrics be the same as those governing the ILEC's performance in provisioning the UNE-P – which is precisely the type of “seamless, low-cost process” that the *Triennial Review Order* sought to establish for hot cuts. *Id.* ¶¶ 200-01. Using the UNE-P as a standard is necessary to ensure that a loop is cut over “as promptly and efficiently as incumbent LECs can transfer customers using unbundled local circuit switching,” as the *Triennial Review Order* requires. *Id.* ¶ 201; *Triennial Review Order* ¶ 512 n.1574.

VI. STATE COMMISSIONS ARE PERMITTED TO SET PRICES AND TERMS FOR § 271 ELEMENTS PURSUANT TO FEDERAL AND STATE LAW.

With respect to the *Notice*'s request (¶ 11 nn.38-39) for comment on “the relationship between UNEs and . . . BOC section 271 access obligations,” it is clear that state commissions are permitted to set prices and terms for § 271 elements pursuant to federal and state law. As AT&T has explained in detail in opposing a petition filed by BellSouth asking the Commission to preempt state commissions,⁷⁹ § 271 does not oust state commissions of jurisdiction. State commissions, in the context of resolving interconnection disputes under § 252 or under state law, plainly retain authority to set the prices and terms for § 271 elements in the first instance.

Under § 271, the Commission's federal interest is to ensure that state commission-set rates for checklist items are not too *high*, but there is absolutely no § 271 basis for a federal concern that these rates are too *low*. Some of the Bells, nonetheless, have argued that the Commission is the *exclusive* entity to set, in each state, the rates, terms, and conditions for all of the items in the competitive checklist that are not unbundled under § 251. Neither the terms nor the purposes of § 271 support the Bells' position. Section 271 provides that the Commission is

⁷⁹ Comments of AT&T Corp. (filed in WC Docket No. 04-245, July 30, 2004).

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the exclusive arbiter of a Bell company's *application* to provide in-region, interLATA service in a state, 47 U.S.C. § 271(d)(3), but it nowhere provides the Commission with exclusive ratemaking authority over services provided pursuant to the competitive checklist or preempts state commissions from exercising authority they otherwise have been granted under federal or state law. *See WorldCom, Inc. v. FCC*, 308 F.3d 1, 7 (D.C. Cir. 2002) (it is not reasonable to "expect the § 271 process to grow into a full-scale ratemaking on the part of the FCC").

The Commission's role under § 271 is to examine competitive conditions in a state's local markets, including the interconnection agreements that the state commission has approved and that the Bell has implemented, and to determine whether the Bell has met all of the conditions of the checklist and whether local competition in the state is sufficiently developed so that Bell entry into interLATA markets meets the public interest. *See, e.g., AT&T Corp. v. FCC*, 220 F.3d 607, 631-32 (D.C. Cir. 2000) (a § 271 proceeding is "focused on an individual applicant's performance" and the Commission's "judgment about the current state of competition in local markets"). Under § 271, therefore, all that the Commission is concerned with is whether these minimum § 271 conditions are satisfied (and continue to be satisfied), so that the Bell may properly be authorized to provide in-region, interLATA services in the state. As the Commission has repeatedly stressed, in making its § 271 inquiries, it is indifferent to the particular rates for individual checklist items that have been developed in a state, so long as those rates are not shown to be so high as to exceed the upper bounds of the federal rate standard. Not surprisingly, then, the Commission did not undertake the task of setting particular and specific rates for the competitive checklist items when reviewing § 271 applications. *See Sprint Comm. Co. v. FCC*, 274 F.3d 549, 556 (D.C. Cir. 2001) ("When the Commission adjudicates § 271 applications, it does not – and cannot – conduct de novo review of state rate-setting

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determinations”); *AT&T Corp*, 220 F.3d at 615 (“The FCC does not conduct de novo review of state pricing determinations in section 271 proceedings, nor does it adjust rates . . .”); *California 271 Order* ¶ 41 (“we perform our section 271 analysis based on the rates before us”). Rather, the Commission merely reviewed the rates that state commissions set for compliance with minimum federal standards, and it approved applications even though rates for local services varied tremendously from state to state. *See, e.g., Sprint*, 274 F.3d at 559 (finding that a section 271 application for Kansas complied with the checklist even though some charges “remain significantly higher in Kansas than in Texas”); *California 271 Order* ¶ 64 (finding that, under the Commission’s “benchmark[ing]” approach, a 30 percent difference between loop rates in two states is acceptable to show compliance).

Further, the Commission did not contemplate a different role by its holding in the *Triennial Review Order* that, when § 271 checklist items are not required to be unbundled under § 251, a Bell is entitled to offer prices, terms, and conditions that meet the “just, reasonable and nondiscriminatory” standards contained in §§ 201 and 202 of the Act. *Triennial Review Order* ¶¶ 656-64. All that this means is that the Commission retains ultimate authority to make a determination pursuant to § 271(d)(6) whether a particular rate charged by the Bell is so high (as judged by §§ 201 and 202’s standards) that the Bell is no longer in compliance with § 271’s requirements. The *Triennial Review Order* language does not indicate that the Commission would in the first instance set all of these rates in all of the Bell states, or that the states would be preempted from setting rates.

There is also no merit to the claim that Congress provided states only a consultative role under § 271. In fact, the text of § 271 demonstrates that Congress fully expected that state commissions would in the first instance set the particular rates for competitive checklist items.

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Under the terms of § 271(c)(1)(A) and § 271(c)(2)(A), which is entitled “Agreement required,” before a Bell can offer in-region, interLATA services in a state, it must satisfy the express condition that it provide the competitive checklist items (§ 271(c)(2)(B)) through “binding agreements that have been approved *under section 252.*” 47 U.S.C. §§ 271(c)(1)(A); 271(c)(2)(A) (emphasis added). Where negotiations fail, it is the state commissions that must conduct arbitrations pursuant to § 252 to form an interconnection agreement that can be approved “under section 252.” A Bell can thus comply with its § 271 duties *only* by entering into interconnection agreements “under section 252” (§ 271(c)(1)(A)) that specify terms and conditions for § 271’s checklist items. In arbitrating interconnection agreements, state commissions plainly will in the first instance set the rates, terms, and conditions for § 271 checklist items. *See Sprint*, 274 F.3d at 552 (noting that the competitive checklist requirements are “enforced by state regulatory commissions pursuant to § 252”).

The Commission has also always recognized that it is essential that the Bells demonstrate compliance with § 271 through binding and lawful § 252 interconnection agreements that contain specific terms and conditions implementing the competitive checklist. For example, the Commission has dismissed § 271 applications and determined that a Bell fails to comply with the checklist if it relies on an agreement that is not in fact binding and is not approved by the state commission. *See, e.g., First Application of Ameritech Michigan* ¶ 22; *see also Michigan 271 Order* ¶¶ 25, 71. The Commission has also made clear that when a competitive carrier requests a particular checklist item, a Bell “is providing” that item and complies with § 271(c)(2)(A) only if it has a “concrete and specific legal obligation to furnish the item upon request *pursuant to state-approved interconnection agreements that set forth prices and other terms and conditions.*” *Id.* ¶ 110 (emphasis added).

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Accordingly, in order for the Bells to come into – and to remain in – compliance with the § 271 checklist, they are required to negotiate and then arbitrate interconnection agreements before state commissions that contain terms and conditions for each of the section 271 checklist items. If a Bell refuses to do so and thus does not enter into binding interconnection agreements regarding the § 271 network elements listed in the checklist, then the Bell would plainly have “ceased to meet” one of the essential conditions of § 271, § 271(d)(6); *see* § 271(c)(2)(A) (entitled “Agreement *required*”) (emphasis added).

As § 271 indicates, the Act provides states with express authority under federal law and permits the states to exercise authority they retain under state law to set rates for checklist items. Congress provided that, when conducting arbitration proceedings instituted pursuant to § 252, state commissions “shall resolve each issue set forth in the petition [for arbitration] and the response.” 47 U.S.C. § 252(b)(4)(C). Thus, when a party seeks arbitration, it first must provide documentation concerning “the unresolved issues,” which then become subject to arbitration before the state commission. *Id.* § 252(b)(2)(A)(i). It is these “unresolved” issues between the parties that the state commissions must decide under the procedures and timeframes specified in § 252. And, as just described above, the Act expressly contemplates that the unresolved issues to be decided in § 252 arbitrations would include determinations regarding the rates, terms, and conditions of § 271 checklist items.

Federal courts have uniformly held that state commissions are authorized to decide – indeed, must decide – all “open issues” in a § 252 arbitration proceeding, which can include, for example, issues of state law and § 271 checklist items. For example, the Fifth Circuit reversed a state commission’s reasoning for refusing to arbitrate an issue in these circumstances. *See Coserv Ltd. Liability Corp. v. Southwestern Bell Tel. Co.*, 350 F.3d 482 (5th Cir. 2003). It held

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that a state commission “err[s]” whenever it “narrowly” interprets § 252 to permit the state commission to decide only issues related to § 251(b) and (c). *Id.* at 486, 488. Rather, the Court stated that, in seeking to reach an interconnection agreement, the “parties are free to include interconnection issues that are not listed in § 251(b) and (c) in their negotiations. . . . [N]othing in § 252(b)(1) limit[s] open issues only to those listed in § 251(b) and (c).” *Id.* at 487. As the Fifth Circuit found, Congress expected that negotiations initiated pursuant to § 252 might expand to include “other issues” that would be “link[ed] . . . together under the § 252 framework,” and Congress “still provided that *any issue* left open after unsuccessful negotiation would be subject to arbitration.” *Id.* Accordingly, the Court concluded that, where the “parties have voluntarily included in negotiations issues other than those duties required of an ILEC by § 251(b) and (c), those issues are subject to compulsory arbitration.” *Id.*; accord *MCI Telecom. Corp. v. BellSouth Telecom. Inc.*, 298 F.3d 1269, 1274 (11th Cir. 2002) (recognizing that state commissions can decide issues that the parties agree to negotiate).

In addition to the authority that state commissions have to determine “unresolved” issues in an arbitration, § 252(e)(3) makes it explicit that, subject to § 253, “*nothing* in” § 252 – including, for example, the provisions in § 252(b)(4)(A) providing that state commissions must limit its arbitration proceeding to the issues raised by the arbitration petition – “shall prohibit a State commission from establishing or enforcing other requirements of State law *in its review of an agreement.*” 47 U.S.C. § 252(e)(3) (emphasis added). Thus, regardless of the open issues presented by the parties to an arbitration or the scope of an incumbent’s duty to negotiate, Congress unmistakably provided that, during the course of serving as an arbitrator under § 252, a state commission is always entitled to establish or enforce pro-competitive state law requirements in an interconnection agreement in addition to implementing federal

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requirements.⁸⁰ With respect to checklist items that the Bells make available pursuant to § 271 but not § 251, the states clearly retain authority under state law to set particular prices for these items.

The Bells apparently believe that, if the Commission attempts to preempt the state commissions, then it will facilitate “commercial negotiations” between the Bells and new entrants for the § 271 elements. But the Act already leaves ample room for the parties to negotiate rates pursuant to interconnection agreements. *See* 47 U.S.C. § 252(a)(1). And, as the dominant providers of local services, the Bells have absolutely no incentives to negotiate reasonable rates for § 271 checklist items that are not also required under section 251 – particularly since all of the Bells have already been granted interLATA authority, which was one of the Act’s principal incentives for the Bells to comply with their market-opening obligations. *See Local Competition Order* ¶ 55 (“We find that incumbent LECs have no economic incentive, independent of the incentives set forth in section 271 and 274 of the 1996 Act, to provide potential competitors with opportunities to interconnect with and make use of the incumbent LEC’s network and services”). Accordingly, if the Commission attempts to preempt state commissions from exercising their authority to set rates for checklist items, it would not encourage negotiated solutions; rather, it would, in fact, only further discourage the Bells from participating in good faith negotiations.

⁸⁰ Once again, the decision in *Coserv* also makes clear that the Bells can be required by state law to negotiate and arbitrate issues that fall outside the scope of § 251(c), including the terms and conditions applicable to § 271 network elements that are not subject to unbundling by the Commission under § 251(d)(2). *See Coserv*, 350 F.3d at 487-88 (if an issue is not subject to arbitration pursuant to § 252, it can “become subject to appropriate state remedies;” these “other issues” can then be “link[ed] . . . together under the § 252 framework”). Thus, even if an incumbent has no duty to negotiate an issue under federal law, it can be required to do so under state law.

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Ultimately, in order to prevent the Bells from stifling local competition by shirking their § 271 duties, new entrants, if denied the opportunity to arbitrate these issues before state commissions, would be forced to file a flood of complaints at the Commission pursuant to § 271(d)(6) of the Act – which requires complete resolution of such complaints in *90 days*. See 47 U.S.C. § 271(d)(6). Thus, the practical effect of any decision that purported to preempt state commissions would be to force the Commission to set rates, on an expedited basis, in each of the states and for each of the items that Bells must provide under the competitive checklist.⁸¹

VII. MERGER CONDITIONS BIND VERIZON AND SBC TO PROVIDE UNES.

In response to the Commission’s request for “comment on any other issues the Commission should address in light of *USTA II*,” Notice ¶ 11, AT&T submits that the Commission should find that Verizon and SBC are bound by merger conditions to offer access to UNEs and UNE combinations.

The Commission found that the proposed mergers of Bell Atlantic with GTE and of SBC with Ameritech posed “significant potential public interest harms” because each proposed transaction would remove an actual potential entrant; eliminate a “benchmark;” and “increas[e] the incentive and ability of the merged entity to discriminate against rivals, particularly with respect to advanced services” – harms “not mitigated by the proposed transaction’s potential public interest benefits.” *Bell Atlantic/GTE Merger Order* ¶ 247; *SBC/Ameritech Merger Order* ¶ 348. The Commission ultimately agreed to approve these mergers, and found that both of “proposed transaction[s], on balance . . . serve[d] the public interest, convenience and necessity,” but only because of the applicants’ “ongoing compliance” with the conditions agreed to by

⁸¹ Alternatively, the Commission would need to address the same issues in a rulemaking of general application.

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merged entities. *Bell Atlantic/GTE Merger Order* ¶ 250 (emphasis added); *SBC/Ameritech Merger Order* ¶ 359.

One of the central purposes of the merger conditions was to protect local competition given the uncertainty surrounding the Commission unbundling rules. To address this, SBC and Verizon each agreed “to reduce uncertainty to competing carriers from litigation that may arise in response to the FCC’s order in its UNE Remand proceeding,” and SBC agreed that it would provide UNEs:

under the same terms and conditions that such UNEs or combinations of UNEs that were made available on January 24, 1999, . . . until the earlier of (i) the date the Commission issues a final order in its UNE remand proceeding in CC Docket No. 96-98 finding that the UNE or combination of UNEs *is not required to be provided* by SBC/Ameritech in the relevant geographic area, or (ii) the date of a final, non-appealable judicial decision providing that the UNE or combination of UNEs *is not required to be provided* by SBC/Ameritech in the relevant geographic area. This Paragraph shall become null and void and impose no further obligation on SBC/Ameritech after the effective date of a final and non-appealable Commission order in the UNE remand proceeding.

SBC-Ameritech Merger Order, App. C, ¶ 53 (emphases added, footnote omitted).⁸² In both cases, these merger conditions continue to apply and require Verizon and SBC to provide UNEs and UNE combinations in their operating territory. As an initial matter, these conditions were

⁸² The merger condition in the Bell Atlantic-GTE merger (Merger Condition XIII) states that Verizon will continue to provide

the UNEs and UNE combinations required in [the UNE Remand Order and Line Sharing Order] in accordance with those orders until the date of a final, non-appealable judicial decision providing that the UNE or combination of UNEs is not required to be provided by Bell Atlantic/GTE in the relevant geographic area. The provisions of this Paragraph shall become null and void and impose no further obligation on Bell Atlantic/GTE after the effective date of final and non-appealable orders in the UNE Remand and Line Sharing proceedings, respectively.

Bell Atlantic/GTE Merger Order, App. D, ¶ 39.

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effectively drafted by SBC and by Verizon, and any ambiguity must be construed against them. *See United States v. Seckinger*, 397 U.S. 203, 210 (1970) (“[A] contract should be construed most strongly against the drafter”). In any event, under any reading of these contractual provisions, SBC and Verizon remain obligated to provide existing UNEs and UNE combinations; there is no conceivable counter-argument.

First, neither merger condition is subject to the more general three-year sunset that applies to other merger conditions. The default sunset provision does not apply to conditions that have their own specific termination language. *See SBC/Ameritech Merger Conditions Order* ¶ 3 (“Some of the [merger] conditions . . . are not subject to that expiration date because the condition itself specifically establishes its own period of applicability.”). The Enforcement Bureau has already expressly recognized that the UNE condition is a condition that is *not* subject to the three year sunset period. *See id.* ¶ 3 n.7.

These merger conditions are still in effect because there is no “final and non-appealable Commission order in the UNE remand proceeding.” This reading is compelled by the Commission’s explanation of this merger condition: that “from now until the date on which the Commission’s order in that proceeding, *and any subsequent proceedings*, becomes final and non-appealable,” SBC and Verizon “will continue to make available to telecommunications carriers each UNE that was” previously available. *SBC/Ameritech Merger Order* ¶ 394; *Bell Atlantic/GTE Merger Order* ¶ 316. In the wake of the *USTA II* decision, there are still “subsequent proceedings” underway at the Commission, and the Commission has yet to issue a final, non-appealable order determining whether SBC and Verizon must make a number of important UNEs, including switching, available. Thus, the condition is still operative.

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Contrary to the arguments previously made by SBC, these merger conditions did not terminate when the D.C. Circuit issued its *USTA I* decision. As an initial matter, that argument has been rejected by federal courts.⁸³ In *Michigan Bell Tel. Co. v. Chappelle*, 222 F. Supp. 2d 905 (E.D. Mich. 2002), *aff'd*, 93 Fed. Appx. 799 (6th Cir. 2004), the district court reviewed the merger conditions and expressly held that that they must be enforced, even if the Commission has removed any independent obligations to provide competitors access to certain UNEs. *Id.*; *accord Wisconsin Bell v. AT&T*, Slip Op. at 17 (finding no “basis to absolve plaintiff [SBC] from abiding by the terms of its Merger Agreement”).⁸⁴

Further, any argument that the merger conditions sunset after *USTA I* would render the Commission’s phrase “any subsequent proceedings” superfluous. The *UNE Remand Order* was reversed by *USTA I*, and the *Triennial Review Order* was the Commission’s order on remand from that decision.⁸⁵ Given that the *UNE Remand Order* was issued prior to the issuance of the *SBC/Ameritech Merger Order* and the *Bell Atlantic/GTE Merger Order*, it would have been a simple matter for the Commission (or the applicants) to write the condition to specify that the

⁸³ *Michigan Bell Tel. Co. v. Chappelle*, 222 F. Supp. 2d 905 (E.D. Mich. 2002), *aff'd*, 93 Fed. Appx. 799 (6th Cir. 2004); *Wisconsin Bell, Inc. v. AT&T*, No. 03-C-671S, (W.D. Wis. July 1, 2004) (“*Wisconsin Bell v. AT&T*”).

⁸⁴ The Commission also has concluded that the *Merger Order* requires SBC to provide competitive carriers with unrestricted access to the UNEs that SBC agreed to provide in the merger agreement. Indeed, the Commission recently imposed a \$6 million fine on SBC for violating paragraph 56 of the *Merger Order* by restricting the use of certain UNEs. *SBC Shared Transport NAL* ¶ 1.

⁸⁵ The *Triennial Review Order* is expressly captioned as an “Order on Remand” in both the *UNE Remand* docket (CC Docket No. 96-98) and the *Line Sharing* docket (CC Docket No. 98-147). And that is, of course, why the appeal of the *Triennial Review Order* was transferred from the Eighth Circuit to the D.C. Circuit and assigned to the same panel that heard *USTA I* – at the request of SBC and Verizon.

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obligation to offer UNEs would exist until the pending judicial review of the *UNE Remand Order* was final. The Commission, however, did not adopt such language. Rather, as noted, the plain language of the merger condition provides that the commitment to offer UNEs applies until there is a “*final and non-appealable Commission order[]* in the UNE Remand proceeding.” *SBC/Ameritech Merger Order*, App. C, ¶ 53 (emphasis added); *Bell Atlantic/GTE Merger Order*, App. D., ¶ 39. Further, the Commission, in explaining this condition, expressly stated that the condition would apply “until the date on which the Commission’s order in that proceeding [UNE Remand], and any subsequent proceedings, become final and non-appealable.” *SBC/Ameritech Merger Order* ¶ 394 (emphasis added); *Bell Atlantic/GTE Merger Order* ¶ 316. Under the reading that SBC and Verizon have advocated, there would never be any “subsequent proceedings” because the obligation would terminate after the initial review of the *UNE Remand Order*. See also *Bell Atlantic/GTE Merger Order* ¶ 316 (UNE condition would have no “practical effect” unless the *UNE Remand Order* or *Line Sharing Order* were “stayed or vacated” (emphasis added)).

Nor is it the case that this condition terminates when *USTA II* becomes final. In *USTA II*, the court did not hold that incumbents “are not required” to provide UNEs within the meaning of the condition. Rather, the court vacated the unbundling rules a second time merely for lack of reasoned explanation, which has triggered another “subsequent proceeding” on remand which is still pending at the Commission. There is still no final, non-appealable order with respect to the aspects of the Commission’s unbundling rules that were vacated in *USTA II*. The very point of the condition was to preserve the *status quo* should a court stay or vacate the unbundling rules that the Commission adopted in the UNE proceeding – as the D.C. Circuit has done in *USTA II*. *SBC/Ameritech Merger Order* ¶ 394; *Bell Atlantic/GTE Merger Order* ¶ 316.

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Accordingly, any contention that the merger conditions have been satisfied, notwithstanding the current uncertainty regarding the scope of the incumbents' unbundling obligations, would be contrary to the text and to the entire purpose of these conditions. The Commission found both that these mergers would reduce local competition and that affirmative steps were necessary to facilitate UNE-based competition. In particular, the Commission recognized that local competition was unlikely if carriers did not have a clear entitlement to particular UNEs. *SBC/Ameritech Merger Order* ¶ 394; *Bell Atlantic/GTE Merger Order* ¶ 316. Thus, the intended purpose of the condition was to provide the necessary certainty to induce local entry. *SBC/Ameritech Merger Order* ¶ 394; *Bell Atlantic/GTE Merger Order* ¶ 316. And it does so by ensuring that the incumbent remains obligated to provide UNEs until litigation surrounding the *UNE Remand Order* is finally resolved, by either: (1) a final judicial decision upholding the unbundling rules that the Commission issues in those proceedings; (2) a final, non-appealable Commission order eliminating unbundling of a particular UNE; or (3) a final judicial decision holding that the Commission cannot require unbundling of a particular element. Because none of those conditions is satisfied, application of this condition is mandatory.

VIII. STATE COMMISSIONS ARE NOT PREEMPTED BY THE FCC REGULATIONS AND CAN SUPPLEMENT FEDERAL REQUIREMENTS WITH PRO-COMPETITIVE UNBUNDLING RULES ISSUED UNDER STATE LAW.

The Commission should also “address in light of *USTA II*” (*Notice* ¶ 11) the effect of the Commission’s unbundling rules on the authority of state commissions to adopt unbundling requirements pursuant to federal and state law. Particularly since the *Triennial Review Order*, the incumbents have taken absurdly aggressive positions that eviscerate state commissions’ authority and that assert that federal law essentially occupies the field of unbundling regulations. Even though the Act adopts minimum federal requirements that set a “floor below which . . . [a state] may not go” and that do not affect the authority of states to adopt additional

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procompetitive requirements under state law,⁸⁶ these incumbents have asserted that state commissions are forbidden from imposing unbundling obligations – even when the Commission has not addressed the relevant element one way or the other. This view is unsupported by the Act, and the Commission should expressly endorse state commission orders that add or supplement unbundling obligations.

Prior to the 1996 Act, states had exclusive jurisdiction over local telephone competition, 47 U.S.C. § 152(b), and some states had already adopted local competition measures. When federal law enters an area previously subject to state regulation, there is a particularly strong “presumption” that Congress did not mean to oust state law. *See Cipollone v. Liggett Group, Inc.*, 505 U.S. 504, 518 (1992). And it is clear that the 1996 Act did not “intend . . . to disrupt the pro-competitive actions some states already ha[d] taken” or that other states would take. *Local Competition Order* ¶ 62. Rather than displace state authority generally, the 1996 Act expressly preempts only state law entry barriers, *see* 47 U.S.C. § 253(b), while enacting four separate savings clauses that authorize states to enact or enforce additional procompetitive requirements under state law so long as they do not “lower” the federal floor.⁸⁷ The 1996 Act is therefore analogous to the numerous other federal statutes that place a floor under state regulation of the same subjects but not a ceiling above them.⁸⁸

⁸⁶ *Iowa Utilities Bd. v. FCC*, 120 F.3d 753, 806-07, 812 (8th Cir. 1997) (“*IUB I*”) (subsequent history omitted).

⁸⁷ 47 U.S.C. §§ 251(d)(3), 252(e)(3), 261(b), 261(c); *see also CSX Transp., Inc. v. Easterwood*, 507 U.S. 658, 664 (1993) (savings clauses are “the best evidence of Congress’ pre-emptive intent”).

⁸⁸ *See, e.g., Atherton v. FDIC*, 519 U.S. 213, 216 (1997) (“We conclude that state law sets the standard of conduct as long as the state standard (such as simple negligence) is stricter than that of the federal statute. The federal statute nonetheless sets a ‘gross negligence’ floor, which applies as a substitute for state standards that are more relaxed.”); *Old Bridge Chems., Inc. v.*
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That the Commission’s regulations serve as a federal floor below, not a ceiling above, state unbundling orders is well illustrated by the Fifth Circuit’s decision in *Southwestern Bell Tel. Co. v. Waller Creek Communications, Inc.* In that case, the incumbent challenged a decision by the state commission ordering it to combine network elements for a competitor. *See* 221 F.3d at 820. The incumbent contended that this decision was “illegal” because it was based on a Commission regulation specifying when incumbents had to combine elements, and that regulation had been vacated by the Eighth Circuit. *See id.* The Fifth Circuit rejected the argument: “Nothing in the [1996 Act] forbids such combinations. Even if the Eighth Circuit’s decision on this issue is correct – which we do not decide today – it does not hold that such arrangements are prohibited; rather, it only holds that they are not required by [federal] law.” *Id.* at 821. It is simply not possible to square this binding precedent with the view that whatever federal law does not require it forbids.⁸⁹

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New Jersey Dep’t of Env’tl Prot., 965 F.2d 1287, 1292 (3d Cir. 1992) (“[A]lthough waste management may be an area of overriding national importance, in legislating in this field Congress has set only a floor, and not a ceiling, beyond which states may go in regulating the treatment, storage, and disposal of solid and hazardous wastes.”); *United States v. Akzo Coatings of Am., Inc.*, 949 F.2d 1409, 1454-45 (6th Cir. 1991) (CERCLA savings clause, 42 U.S.C. § 9614(a), like § 252(e)(3), permits states to impose “additional . . . requirements” beyond federal law; “CERCLA sets only a floor, not a ceiling, for environmental protection. Those state laws which establish more stringent environmental standards are not preempted by CERCLA.”); *Wastak v. Lehigh Valley Health Network*, 342 F.3d 281, 295 n.8 (3d Cir. 2003) (Older Workers Benefit Protection Act “was enacted to establish a floor, not a ceiling” (internal quote marks and alterations omitted)). These decisions recognize the general principle that “a state or locality’s imposition of additional requirements above a federal minimum is unlikely to create a direct and positive conflict with federal law.” *Southern Blasting Servs., Inc. v. Wilkes County, N.C.*, 288 F.3d 584, 591 (4th Cir. 2002).

⁸⁹ Similarly, in *MCI Telecomms. Corp. v. U. S. West Comm.*, 204 F.3d 1262 (9th Cir. 2000), the Ninth Circuit upheld the state’s new combinations requirements (even though the parallel federal rules had been vacated) because, rather than “violate[]” the Act, they are procompetitive and a reasonable means of preventing discrimination. *Id.* at 1268. The Court took explicit note of the
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As the Sixth Circuit explained after reviewing the 1996 Act savings clauses, Congress expressly “authorized states to implement additional requirements that would foster local interconnection and competition, stating that the Act does not prohibit state commission regulations ‘if such regulations are not inconsistent with the provisions of [the 1996 Act].’” *Michigan Bell Tel. Co. v. MCIMetro Access Trans. Servs., Inc.*, 323 F.3d 348, 358 (6th Cir. 2003) (*quoting* 47 U.S.C. § 261). State commissions thus retain “independent authority” to impose regulatory measures that they “find . . . to be in the public interest and a means of promoting competition.” *Indiana Bell Tel. Co. v. McCarty*, 362 F.3d 378, 391-93 (7th Cir. 2004). This is true even when “the FCC in its role as federal regulator” does not impose the measure.

Although the 1996 Act broadly delegates federal authority to the state commissions (*e.g.*, § 252), Congress was explicit that this federal authority is not the only source of state power to regulate local services and facilities. Rather, state commissions may also act pursuant to independent state-law authority. *See Triennial Review Order* ¶ 186 (describing the two distinct sources of state commission authority). In enacting the 1996 Act, Congress noted with approval ongoing state efforts to “open the local networks of telephone companies,” S. Rep. No. 104-23 at 5 (1995), and endeavored to build on these state efforts – not kill them.

Congress’s intent to preserve state-law authority is evinced by four separate anti-preemption “savings” clauses – all of which make it crystal clear that nothing in the statute impedes the states’ ongoing efforts to open their local markets to competition. First, the Act

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fact that in addition to the states’ right to implement federal law, the Act generally “reserves to states the ability to impose additional requirements [under state law] so long as the requirements are consistent with the Act and ‘further competition.’” *Id.* at 1265.

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provides that “notwithstanding” the limited federal standards in § 252(e)(2) for rejecting negotiated and arbitrated ICAs, “nothing in this [§ 252] shall prohibit a State commission from establishing or enforcing other requirements of State law in its review of an agreement.” 47 U.S.C. § 252(e)(3). Congress preserved this authority with only one qualification: the state commission may enforce or establish state law requirements “subject to section 253 of this title,” *id.*, which prohibits states from imposing legal requirements that create barriers to competitive entry. Thus, so long as it does not invoke state law to create barriers to entry in violation of section 253, and so long as its regulations are not inconsistent with the Act’s pro-competitive requirements, a state may exercise its inherent sovereign power to regulate intrastate facilities and services, including the terms of competitive access to local telephone networks.⁹⁰ Section 252(e)(3) represents “an explicit acknowledgment that there is room in the statutory scheme for autonomous state commission action.” *Puerto Rico Tel. Co. v. Telecomm. Regulatory Bd.*, 189 F.3d 1, 14 (1st Cir. 1999).

Second, § 251 bars the Commission from doing anything to block such pro-competitive state-law requirements. That section, when read in conjunction with § 252 and § 253, sets up the Commission’s regulations as no more than minimum national floors. While § 251(d)(1) requires the Commission to adopt regulations to implement the unbundling and other requirements of § 251, § 251(d)(3) limits the Commission’s ability to preempt state law when doing so.

⁹⁰ See *Southwestern Bell Tel. Co. v. Public Util. Comm’n*, 208 F.3d, 475, 481 (5th Cir. 2000) (§ 252(e)(3) “obviously allows a state commission to consider requirements of state law when approving or rejecting interconnection agreements”); *AT&T Communications v. BellSouth Telecomms., Inc.*, 238 F.3d 636, 642 (5th Cir. 2001) (“Subject to § 253, the state commission may also establish or enforce other requirements of state law in its review of an agreement.”); *AT&T Communications of N.J., Inc. v. Bell Atlantic-N.J., Inc.*, No. Civ. 97-CV-5762(KSH), 2000 WL 33951473, at *14 (D.N.J. Jun. 6, 2000) (“§ 252(e)(3) gives states the authority to impose unbundling requirements beyond those mandated by FCC regulations.”).

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Section 251(d)(3), entitled “Preservation of State access regulations,” bars the Commission from “prescribing” or “enforcing” regulations under section 251 that “preclude the enforcement of *any regulation, order, or policy of a State*,” so long as those state measures are “consistent with the requirements of this [§ 251],” and do “not substantially prevent implementation of the requirements of this section and the purposes of this part [of the Act].” 47 U.S.C. § 251(d)(3)(B) & (C) (emphasis added).

The plain language of this provision belies the claim that *any* state unbundling requirement that is different from the Commission requirement necessarily conflicts with, or substantially prevents implementation of, the Act. If every unbundling requirement different from a Commission regulation were preempted, then the language requiring specific Commission action to “preclude the enforcement” of state law based on specified findings would be negated. Moreover, even if the Commission were some day to attempt to satisfy the requirements of § 251(d)(3) and preempt a state unbundling decision, it could do so only on the basis that the state action conflicted with § 251 of the 1996 Act, *not* Commission regulations implementing it. Section 251(d)(3) expressly bars the Commission from adopting regulations that preempt a state access or interconnection requirement that is “consistent with the requirements of *this section*” and does not “substantially prevent implementation” of these requirements or “the purposes of this part,” *i.e.*, §§ 251-61, *of the Act*. Because § 251(d)(3) limits the Commission’s authority to adopt preemptive regulations, the lawfulness of a state measure providing for additional unbundling is measured against the requirements and purposes of § 251 of the *Act*, not those of the *Commission’s regulations*.

Third, lest any doubt remain concerning preservation of state authority to adopt pro-competitive state-law requirements that go beyond the federal floor, § 261(c) provides that

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“[n]othing in this part precludes a State from imposing requirements on a telecommunications carrier for intrastate services that are necessary to further competition in the provision of telephone exchange service or exchange access, as long as the State’s requirements are not inconsistent with this part or the Commission’s regulations to implement this part.” 47 U.S.C. § 261(c).⁹¹

Fourth, in § 601(c)(1) of the Act, Congress provided courts with a special rule of construction in interpreting the Act so as to preserve state authority. Congress specified that the “Act shall not be construed to modify, impair, or supersede . . . State[] or local law unless expressly so provided.” Act § 601(c)(1), 110 Stat. at 143 (uncodified note to 47 U.S.C. § 152). Congress included this clause to “prevent[] affected parties from asserting that the [Act] impliedly pre-empts other laws.” H.R. Conf. Rep. No. 104-458, at 201 (1996), *reprinted in* 1996 U.S.C.C.A.N. 124, 215.⁹²

⁹¹ The word “inconsistent” (like the word “consistent” in § 251(d)(3)) is a term of art in preemption law, and Congress’s deliberate decision to use it has to be given effect. *See McDermott Int’l, Inc. v. Wilander*, 498 U.S. 337, 342 (1991) (“In the absence of contrary indication, we assume that when a statute uses such a term, Congress intended it to have its established meaning.”). In particular, because the Supreme Court has held that state regulations are “consistent” with federal law so long as it is “possible to comply with the state law without triggering federal enforcement action,” *Jones v. Rath Packing Co.*, 430 U.S. 519, 540 (1977), § 261(c) bars only state measures that would require incumbents to violate the Act or would legally preclude competitors from obtaining elements and using them to provide competing services. *See, e.g., E.B. Elliott Adver. Co. v. Metropolitan Dade Cty.*, 425 F.2d 1141, 1150 (5th Cir. 1970) (“The word ‘inconsistent’, as used in [a preemption provision] means contradictory in the sense of legislative provisions which cannot co-exist.”).

⁹² As the Fifth Circuit has explained, § 601(c) squarely “precludes a broad reading of preemptive authority.” *City of Dallas, Tex. v. FCC*, 165 F.3d 341, 348 (5th Cir. 1999); *see also AT&T Communications of Ill., Inc. v. Illinois Bell Tel. Co.*, 349 F.3d 402, 410 (7th Cir. 2003) (§ 601(c) “precludes a reading that ousts the state legislature by implication.”).

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Taken together, the savings clauses cannot be read to prohibit states from imposing duties beyond those required by federal law. When Congress intends federal regulations to operate as both a floor and as a ceiling, it knows how to do so. In such cases, Congress adopts preemption provisions that – in sharp contrast to the terms of the 1996 Act – expressly preclude states from imposing requirements that “differ” from, are “in addition to,” or are not “identical” to, federal obligations.⁹³ The decisive factor here is that Congress did not use any of these time-honored formulations in the 1996 Act. Instead, Congress did exactly the opposite. Rather than bar states from enacting their own additional unbundling requirements or requiring them to be identical to the federal requirements, the 1996 Act *expressly permits* states to impose additional access obligations so long as they are not “inconsistent” with federal law, *see* 47 U.S.C. § 261(c), or create barriers to entry, *see id.* § 253.

If the Commission were to attempt to broadly preempt state law, it would nullify the various savings clauses adopted by the 1996 Act. But that is flatly impermissible. In *Geier v. American Honda Motor Co., Inc.*, 529 U.S. 861 (2000), the Supreme Court made clear that where Congress includes an express savings clause in a statute, that clause must be construed to have independent, operative effect. In that case, the Court held that despite the fact that the underlying statute contained a broadly worded *express* preemption clause, the Court would still

⁹³ *See, e.g.*, Medical Device Amendments Act, 21 U.S.C. § 360k(a)(1) (“no State . . . may establish or continue in effect . . . any requirement which is different from, or in addition to, any requirement applicable under this chapter”); Federal Boat Safety Act of 1971, 46 U.S.C. § 4306 (preempting state “law or regulation . . . that is not identical to a regulation prescribed under section 4302 of this title”); Consumer Product Safety Act, 15 U.S.C. § 2075(a) (“no State or political subdivision of a State shall have any authority [to establish a safety requirement], . . . unless such requirements are identical to the requirements of the Federal standard”); Federal Hazardous Substances Act, 15 U.S.C. § 1261 note (b)(1)(A) (“no State . . . may establish or continue in effect a . . . requirement application . . . unless such . . . requirement is identical to the labeling requirement.”).

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construe a separate “saving provision” so that it would not be “render[ed] ineffectual” and would have substantive significance. *Id.* at 870. Here, the only way to give independent effect to the savings clauses is to acknowledge that individual state commissions are free to impose additional unbundling requirements on their incumbent carriers based on local conditions and their different perceptions of the appropriate tradeoffs.

Despite the Act’s manifest preservation of state law authority to add unbundling requirements, the incumbents have repeatedly and increasingly advocated for expansive preemption of state law. Even requirements that states have imposed in the *absence* of any Commission rule have recently come under attack.⁹⁴ These claims amount to a wildly aggressive – and flatly wrong – argument for field preemption. But “[i]f Congress intended to preempt the field, Congress would not have included section 251(d)(3) in the 1996 Act.” *Triennial Review Order* ¶ 192. Field preemption exists only where the “scheme of federal regulation [is] ... so pervasive as to make reasonable the inference that Congress left no room for the States to supplement it,” or where an Act of Congress “touch[es] a field in which the federal interest is so dominant that the federal system will be assumed to preclude enforcement of state laws on the same subject.” *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947); *English v. General Elec. Co.*, 496 U.S. 72 (1990).

As the Supreme Court has noted, “[t]o infer pre-emption whenever an agency deals with a problem comprehensively is virtually tantamount to saying that whenever a federal agency

⁹⁴ See, e.g., *McCarty*, 362 F.3d at 391-93 (rejecting incumbent challenge that “acceptance testing,” a requirement imposed by a state commission to ensure unbundled loops meet specified quality standards, was preempted); *Michigan Bell Tel. Co. v. Lark*, Civil Action No. 04-60128 (E.D. Mich.) (suit to preempt state commission from implementing improvements to loop provisioning in batch hot cut process).

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decides to step into a field, its regulations will be exclusive. Such a rule, of course, would be inconsistent with the federal-state balance embodied in our Supremacy Clause jurisprudence.” *Hillsborough Cty., Fla. v. Automated Med. Labs., Inc.*, 471 U.S. 707, 717 (1985). In the case of local telephony, no such claim could be made even if the Act’s savings clauses did not exist, given the critical role that states continue to play in the area of telecommunications regulation. *See Puerto Rico Tel.*, 189 F.3d at 8 (the Act is “an exercise in what has been termed cooperative federalism”). In any event, far from occupying the field, the Act self-consciously shares it with sovereign state authorities. *See, e.g.*, 47 U.S.C. §§ 152(b), 261(c); 261(b).

IX. THE COMMISSION CANNOT OVERRIDE CHANGE OF LAW PROVISIONS IN EXISTING INTERCONNECTION AGREEMENTS AND THE BELLS CANNOT CIRCUMVENT THOSE PROVISIONS BY SEEKING “WAIVERS” OF THE COMMISSION’S RULES.

The Bells have once again advocated that the Commission’s order in this proceeding should “address” the effect that a Commission decision to remove an unbundling obligation would have under existing change of law provisions and to establish plan that would “override any change-of-law provisions.”⁹⁵ In addition to this general question, BellSouth has filed what purports to be a petition for waiver of the Commission’s rules on conversion of EELs, but which in fact also seeks to ignore change-of-law provisions. None of the Bells’ requests have the slightest merit.

On the more general issue, the Bells contend that action on their proposal is necessary and proper because competitive carriers could purportedly otherwise use the change of law

⁹⁵ *Ex Parte* Letter of Michael Kellogg, USTA, to Marlene Dortch, FCC (filed in CC Docket No. 01-338, July 7, 2004) (attaching *Ex Parte* Letter of Michael Kellogg, SBC, to Marlene Dortch, (filed in CC Docket No. 01-338, Jan. 21, 2003) (“USTA COL Letter”)); *Ex Parte* Letter of Dee May, Verizon, to Marlene Dortch, FCC (filed in CC Docket No. 01-338, July 28, 2004) (“7/28/04 Verizon Letter”).

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provisions to “extend the prior unbundling regime indefinitely.” *Id.* at 1. The Bells assert that any such result would be “in direct conflict” with the *USTA II* decision, which they claim established that the prior unbundling regime was “unlawful and contrary to congressional intent *ab initio*” – and also with the Commission’s findings under the necessary and impair standards. USTA COL Letter at 1-2 & 4.

The Bells first suggest that the Commission can accomplish this result on the ground that “many” interconnection agreements expressly require reformation of the agreement as soon as the Commission makes any change to its rules (and not until final, judicial review of the new rule). USTA COL Letter at 1-2; 7/28/04 Verizon Letter at 2. That may be true, but “many” interconnection agreements do not so provide. Clearly, the Commission cannot use the existence of such change of law language in some interconnection agreements as a basis for interpreting the meaning of entirely different change of law provisions in other agreements.

The Bells ultimately recognize this too. That is why they fall back to the argument that in these circumstances the *Sierra-Mobile* doctrine gives the Commission the authority to override provisions of state interconnection agreements. *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348, 353-55 (1956); *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 344 (1956). These claims are baseless.

The Commission has no authority under the *Sierra-Mobile* doctrine to override the change of law provisions and to impose specific deadlines on State commissions for eliminating access to particular network elements. The *Sierra-Mobile* doctrine permits a federal agency to override provisions of an agreement only if the agreement is within the federal agency’s exclusive jurisdiction and its provisions have been rendered contrary to the public interest by unforeseen intervening developments. None of these conditions exist. There has been no

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unforeseen development. To the contrary, the change of law provisions were developed to address the very type of change in the law that the Bells predict will now occur. And, because the change of law provisions were adopted to allow modifications of agreements when prior rules are vacated, the Commission cannot override the provisions on the theory that it would be “correct[ing] the consequences of [its] vacated rules.” USTA COL Letter at 4-5; Verizon 7/28/04 at 5.⁹⁶

In any event, even if change of law provisions were inadequate to address some unforeseen issues, there is no basis for the Commission to adopt rules in this proceeding that would override the change of law provisions. The Bells’ claims that the Commission has the authority to override these agreements rest on the so-called *Sierra-Mobile* doctrine. The Bells assert that the doctrine “arguably” gives the Commission the authority to negate any provision of any interconnection agreement that the Commission finds to be contrary to the public interest, USTA COL Letter at 3, and the Bells claim that the Commission has the clear authority to override the change of law provisions because the Commission putatively would here be ““correct[ing] the consequences of [its] vacated rules.”” *Id.* at 4-5; 7/28/04 Verizon Letter at 5. These claims do not have the slightest substance.

⁹⁶ Verizon’s argument that there categorically has been no “change in law” as the term is used in interconnection agreements is also baseless. 7/28/04 Verizon Letter at 3-4. Verizon points merely to the uncontested principle that judicial decisions, including ones that vacate agency rules, are normally retroactive. *Id.* But that only proves the point that there has quite literally been a “change of law.” Prior to the decisions in *USTA I* and *USTA II*, the Commission’s unbundling regulations had not been stayed and, accordingly, were binding and had the force and effect of law. Indeed, that is presumably why the incumbents agreed to provide such UNEs in the interconnection agreements. The vacatur of those unbundling rules changed the law, so that the regulations no longer would be binding. The change in law provisions in interconnection agreements are therefore triggered.

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The *Sierra-Mobile* doctrine applies to regulatory regimes in which privately negotiated contracts are filed with a federal agency and are subject to its plenary authority. The general rule is that a regulated utility that enters into such contracts is not “entitled to be relieved of its improvident bargain,” but that agencies can grant such relief when intervening circumstances which were not foreseen at the time the contract was formed mean that prospective enforcement of the contract in accord with its terms is no longer in the public interest. *Sierra*, 350 U.S. at 355; see *Transmission Access Policy Study Group v. FERC*, 225 F.3d 667, 710 (D.C. Cir. 2000). The necessary conditions for applying *Sierra-Mobile* are not present here.

First, the proposal that the Commission override the change of law provisions and mandate an end to access to particular network elements by particular dates would invade the jurisdiction that the Act confers on State public utility commissions. Under the Act, interconnection agreements are filed with State commissions, not the Commission, for the agreements are subject to state jurisdiction, and the Commission therefore plainly does not have plenary authority to regulate all the rates, terms, and conditions in interconnection agreements. To be sure, § 252(c)(1) requires that the states comply with the Commission’s regulations that implement § 251’s requirements, and, as the Bells correctly state, USTA COL Letter at 5, § 201 of the Act gives the Commission authority to adopt regulations that implement and define § 252(e)(2)’s provisions that allow state commissions to decline to approve negotiated agreements that are discriminatory or contrary to the public interest and to disapprove arbitrated agreements that violate § 251. But, as discussed above, these Commission regulations establish only *minimum* standards to which State commissions must abide. Whether or not Commission regulations authorize particular unbundling requirements, those requirements can be imposed

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under state law so long as they are not inconsistent with the requirements and purposes of the Act itself. *See* §§ 251(d)(3) & 261(b).

For this reason, any attempt by the Commission to negate the change of law provisions and to mandate that State commissions eliminate access to particular unbundled elements by a particular date would exceed the Commission’s jurisdiction under the Act. Regardless of what the Commission’s rules provide, State commissions retain the authority to determine whether access to network elements should be required under state law (or other provisions of federal law), and the Commission cannot prevent State commissions from making such determinations. § 252(e)(3). The change of law provisions are valid incidents to the authority reserved to the states under § 252(e)(3) of the Act, for the change of law provisions are negotiated and State commissions approved mechanisms that allow the State commissions to determine whether, following vacatur of a rule by a court or by the Commission, the same underlying unbundling requirement should be maintained under state or federal law.⁹⁷

Second, even if the Commission had jurisdiction, the *Sierra-Mobile* doctrine would not permit it to override the change of law provisions. The showing the agency must make before invalidating a contractual provision has been characterized as a “heavy burden” that is “much

⁹⁷ In this regard, it is baffling that the Bells attempt to rely (USTA COL Letter at 5) on the Commission’s authority to adopt regulations defining conditions under which states can reject *new* interconnection agreements under § 252(e)(2) on the grounds that they are discriminatory, contrary to the public interest, or contrary to § 251. The change of law provisions here are features of *existing* agreements that previously were approved, so § 252(e)(2)’s criteria are quite irrelevant here. Further, whatever the meaning of § 252(e)(2), § 252(e)(3) says that “nothing in this section [252]” can prohibit states from establishing additional requirements under state law. There is simply no basis for the Commission to assert jurisdiction to negate or otherwise override the change of law provisions in existing interconnection agreements.

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more restrictive” than an ordinary public interest finding in other contexts.⁹⁸ The Commission has explained that “[t]here is a well-established reason why the *Sierra-Mobile* standard for contract reformation is high: preserving the integrity of contracts is vital to the proper functioning of the carrier-to-carrier communications market.”⁹⁹ At a minimum, the doctrine requires “particularized” findings justifying recasting a contract,¹⁰⁰ and courts “stress that generic *Mobile-Sierra* findings are appropriate only in rare circumstances.”¹⁰¹

Here, the Commission could not possibly satisfy the doctrine’s heavy burden. The vacatur of the old rules and the adoption of new ones afford no possible basis for overriding the change of law provisions contained in hundreds of varied contracts between a wide variety of parties. The simple fact is that the change of law provisions were *designed* to address the very intervening circumstance that gives rise to the Bells’ plea: the vacatur of prior rules and the adoption of new unbundling rules. The Bells have provided no conceivable basis for obtaining relief from the contractual provisions they negotiated and agreed to in order to protect their interests in the very circumstances that they anticipated.¹⁰² Thus, in this case, none of the conditions for overriding the terms of interconnection agreements are present.

⁹⁸ See *PEPCO v. FERC*, 210 F.3d 403, 407 (D.C. Cir. 2000) (“much more restrictive” standard than for ratemaking); *Union Pacific Fuels, Inc. v. FERC*, 129 F.3d 157, 168 (D.C. Cir. 1997) (*Mobile-Sierra* power justified “only where the public interest imperatively demands such action) (internal quote omitted); *Papago Tribal Util. Auth. v. FERC*, 723 F.2d 950, 954 (D.C. Cir. 1983) (burden “practically insurmountable”); *ACC Long Distance Corp. v. Yankee Microwave, Inc.*, 10 FCC Rcd. 654, ¶ 17 (1995) (“heavy burden”).

⁹⁹ *IDB Mobile Communications v. COMSAT Corp.*, 16 FCC Rcd. 11474, 11481 (2001).

¹⁰⁰ *Atlantic City Elec. Co. v. FERC*, 295 F.3d 1, 14 (D.C. Cir. 2002).

¹⁰¹ *Transmission Access Policy Study Group*, 225 F.3d at 711.

¹⁰² The Bells claim support from the Commission’s imposition of a “fresh look” requirement on contracts between incumbent LECs and CMRS providers. USTA COL Letter at 3. There, the
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In this regard, there is no substance to the Bells' reliance on *United Gas Improvement Co. v. Callery Props., Inc.*, 382 U.S. 223, 229 (1965). See 7/28/04 Verizon Letter at 5. In that case, the FPC had unlawfully granted certificates that did not limit gas producers to charging prevailing rates, and after the FPC's Order was vacated for that reason, the Supreme Court held that the FPC could retroactively impose that limitation on the certificates. It held that "an agency . . . can undo what is wrongfully done by virtue of its order" that was vacated. But this principle is wholly inapposite here. The change of law provisions do not *implement* the prior unbundling rules that the Bells urge the Commission to supersede and vacate. To the contrary, the change of law provisions enable the Bells to seek *modification* of the interconnection agreements that were based on the to-be vacated rules. Nothing in *Callery* or its progeny justifies any attempt by the Commission to override the change of law provisions.

For these reasons, the Commission may not use the *Mobile-Sierra* doctrine to change contractual provisions in existing interconnection agreements. The same logic also compels the Commission to reject a so-called "waiver" petition by BellSouth, which is nothing more than a more specific version – as applied to EELs conversions that are plainly authorized by the

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Commission found that the LECs had abused negotiating power to "impose[]" on CMRS providers contractual provisions "in violation of" Commission rules. *Local Competition Order* ¶¶ 1094-95. The "fresh look" requirement "addresse[d] inequalities in bargaining power" that had led to this violation and enabled the victims of LEC market power abuses to "negotiate more equitable interconnection agreements." *Id.* ¶ 1095. The Bells – which both have the market power and supported the provisions they now seek to avoid – obviously cannot point to any comparable basis to justify relieving them from their contracts. Moreover, the CMRS fresh look allowed CMRS providers immediately to take advantage of the reciprocal compensation rights that were *minimum* federal requirements. Here, by contrast, minimum federal unbundling requirements will remain in effect, and the change of law provisions afford State commissions an opportunity to determine if the vacatur of prior rules and the adoption of new rules require elimination of access to particular network elements or whether access should continue to be required under provisions of state law that go beyond the minimum federal requirements.

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Triennial Review Order – of their general claim that the Commission can selectively override the change of law provisions.¹⁰³ As discussed above, the Commission is not entitled to change these provisions even if it were to invoke the *Mobile-Sierra* doctrine; *a fortiori*, the Commission cannot merely “waive” the change of law provisions in interconnection agreements to prevent competing carriers from obtaining EELs conversions.¹⁰⁴

BellSouth’s request is that the Commission should allow BellSouth to stop “process[ing] orders” for EELs under the rules announced in the *Triennial Review Order*. BellSouth Pet. at 1. According to BellSouth, this waiver is necessary “to ensure that the revised EEL requirements that allow UNEs to be substituted for special access services are implemented under the schedule anticipated in the *TRO*.” *Id.* at 2. But, unlike other rules promulgated in the *Triennial Review Order*, the Commission made the new EELs rules effective immediately. And the Commission nowhere suggested that it expected the parties to delay in any manner complying with contractual provisions to reform existing interconnection agreements to reflect the new rules. To the contrary, in rejecting BellSouth’s earlier plea for “the extraordinary step of the Commission interfering with the contract process,” *Triennial Review Order* ¶ 701, the Commission set an *outside* limit of 9 months on contract renegotiations, expected negotiations to “commence immediately,” and expressly “admonish[ed] all parties to avoid gamesmanship” that might *delay* implementation of the new rules. *Id.* ¶¶ 703-06 (any delay “will have an adverse impact on

¹⁰³ BellSouth Petition For Waiver (filed in CC Docket No. 01-338, et al., Feb. 11, 2004) (“BellSouth Pet.”).

¹⁰⁴ See Opposition of AT&T To BellSouth Pet. for Waiver, (filed in CC Docket No. 01-338, March 19, 2004) (“AT&T Opp.”); *Ex Parte* Letter of David Lawson, AT&T, to Marlene H. Dortch, (filed in CC Docket No. 01-338, May 7, 2004) (“5/7/04 AT&T Letter”).

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investment and sustainable competition in the telecommunications industry”). BellSouth’s Petition is just such gamesmanship, and the only Commission action that it could properly trigger is “a finding of bad faith” by BellSouth. *Id.* ¶ 706 (“Once the rules established herein are effective, and any applicable change of law process has been triggered, a party’s refusal to negotiate (or actions that would otherwise delay unnecessarily the resolution of) any single issue may be deemed a violation of section 251(c)(1)”). In this regard, the Petition is just one of many steps BellSouth is taking unreasonably to delay its obligations to comply with the Commission’s EELs rules – including, for example, refusing to agree to modify its interconnection agreement with AT&T to include the same EELs language that BellSouth volunteered in an SGAT and claims is compliant with the *Triennial Review Order*. See AT&T Opp. at 3; 5/7/04 AT&T Letter at 2-3.

Although BellSouth purported to justify its waiver request on a need for “a nine month transition period” before converting EELs, Petition at 6, that period has now passed, and, if BellSouth’s views prevail, a waiver could have the effect of stopping all EELs conversions *indefinitely*. That would be an indefensible outcome. Indeed, as the Commission recognized in the *Triennial Review Order* the old EELs rules that the Commission replaced were not operating as the Commission intended and were preventing competitive carriers from purchasing EELs even in circumstances in which the Commission had fully intended since 1996 that EELs be available. Thus, contrary to BellSouth’s suggestions, there has already been far *too much* delay. Given that competitive carriers still do not have access to EELs that should have been available years ago, it is plainly the competitive carriers, not BellSouth and the other incumbents, that are the aggrieved parties here. BellSouth has provided no basis for the Commission to intervene and halt parties from invoking change of law provisions that permit EELs conversions.

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X. THE COMMISSION SHOULD USE ITS BROAD AUTHORITY TO CREATE TRANSITION RULES TO CREATE A MULTI YEAR TRANSITION.

The Commission has clear authority to adopt transitional rules that prevent or minimize disruption caused by “flash cut” changes. To the extent that its unbundling analysis would lead it to make substantial changes from current unbundling rules that might threaten economic dislocation if implemented immediately, the Commission should exercise its authority to phase such changes in over a reasonable transition period.

The courts have repeatedly affirmed the legality of transitional rules to prevent or minimize disruption caused by “flash cut” changes.¹⁰⁵ Such measures are “a standard tool of the Commission.” *Western Union Tel. Co. v. FCC*, 815 F.2d 1495, 1505 (D.C. Cir. 1987). Here, the “at a minimum” language in section 251(d)(2) unquestionably permits the Commission to adopt reasonable transition rules in connection with unbundling determinations. For example, in *USTA I*, the Court expressly “assumed” that the “at a minimum” clause authorized the Commission to order unbundling in conditions when there is no impairment, holding only that the Commission’s “belief” in benefits of the broadest possible unbundling was insufficient to justify the extreme overbreadth that was present in the particular rules that were there at issue. *USTA I*, 290 F.3d at 425. Thus, administrability concerns justify any slight over-inclusiveness of transitional rules.

¹⁰⁵ *Southwestern Bell Tel. Co. v. FCC*, 153 F.3d 523, 538 (8th Cir. 1998) (“[T]his temporary transitional arrangement is not an unreasonable solution to the implicit tension between the FCC’s goals of moving toward cost-based rates and protecting universal service.”); *Rural Tel. Coalition v. FCC*, 838 F.2d 1307, 1315 (D.C. Cir. 1988) (“[T]he allocation is a reasonable measure . . . because it is part of a transitional process, and interim solutions may need to consider the past expectations of parties and the unfairness of abruptly shifting policies.”) (internal quotation marks omitted) (citation omitted); *MCI Telecomm. Corp. v. FCC*, 750 F.2d 135, 142 (D.C. Cir. 1984) (“The phase-out helps to avoid undue economic dislocations.”); *NARUC v. FCC*, 737 F.2d 1095, 1135 (D.C. Cir. 1984) (“[T]he shift from one type of nondiscriminatory rate structure to another may certainly be accomplished gradually to permit (continued . . .)

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To the extent that the Commission does reduce unbundling obligations, it should use that authority to adopt a multi-year transition period to account for the past expectations of parties and the unfairness of abruptly shifting policies. In the time that UNE-P has been truly available, tens of millions of Americans – both residential customers and small businesses receive local services from competing carriers based on UNE-P offerings. It would be irresponsible in the extreme not to provide significant transition period to prevent customer disruption that would result if UNE-P were no longer available. Despite massive efforts, no competitive carrier has been able to deploy its own switches to serve significant numbers of these mass market customers. If unbundled switching were not available, it would take a number of years for the Commission, state commissions, and carriers to eliminate operational barriers to the provision of switch-based services. Accordingly, in these circumstances, a multi-year transition rule would be required. *Cf. CLEC Access Charge Reform Order* ¶ 62 (with respect to changes to competing carriers’ access rates, a three-year “transitional mechanism is vitally important to avoid too great of a dislocation in the CLEC segment of the industry”).

At a minimum, it is undisputed that no incumbent has developed and put into place sufficient “bulk” hot cut procedures that would allow the millions of customers served today via unbundled switching to be transferred efficiently to new facilities-based arrangements without service interruptions. The establishment of an effective, efficient batch cut migration process – “a seamless, low-cost process for transferring large volumes of customers” (*Triennial Review Order* ¶ 422; *see also id.* ¶ 487) as detailed above – is an essential component of any transition from the UNE-P to the provision of service through the competitive carriers’ own facilities.

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the affected carriers, subscribers and state regulators to adjust to the new pricing system.”); *see*
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With respect to the transition for high capacity loops and transport, the Commission should recognize that, particularly in light of the current conditions in the capital markets, it is unrealistic to believe that competitive carriers will be able to self-deploy facilities instantaneously, even when they might not be otherwise impaired. In addition, given that many carriers have entered into long-term contracts to supply services to enterprise customers based upon purchase of EELs at UNE rates, it would plainly be inappropriate for any type of flash cut if access to such UNEs were reduced. *See, e.g., CLEC Access Reform Order* ¶¶ 37, 52, 62 (finding a “three-year transition” in competitive carrier access rates to be appropriate “because it appears to allow sufficient time for CLECs to adjust their business models”); *ISP Inter-carrier Compensation Order* ¶ 83 (three-year ramp down period for reciprocal compensation payments to traffic bound to ISPs); *Access Reform Order* ¶ 46 (“we are concerned that any attempt to move immediately to competitive prices for [certain incumbent access] services would require dramatic cuts in access charges for some carriers. Such an action . . . could prove highly disruptive to business operations”). Accordingly, the Commission should also adopt a multi-year transition period that would apply to any high capacity loops and transport that are not subject to unbundling pursuant to § 251(d)(2).

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also Carrier Identifications Codes Recon Order ¶ 20; *Amendment of Section 64.702 Order* ¶ 71.

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CONCLUSION

In sum, the Commission's choice is not between UNEs and facilities. It is between competition and no competition. This should be an easy choice. Indeed, faithful implementation of the Act permits only one resolution.

Respectfully submitted,

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October 4, 2004

CERTIFICATE OF SERVICE

I hereby certify that on this 4th day of October, 2004, I caused true and correct copies of the forgoing Comments of AT&T to be served on all parties by mailing, postage prepaid to their addresses listed on the attached service list.

Dated: October 4, 2004
Washington, D.C.

/s/ Peter M. Andros

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